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(H.N.S.C No. 104-13): Annual Author...

**ANNUAL AUTHORIZATION OF THE
PANAMA CANAL COMMISSION AND THE
ANNUAL AUTHORIZATION FOR THE
UNITED STATES MARITIME ADMINIS-
TRATION**

HEARING

BEFORE THE

**SPECIAL OVERSIGHT PANEL ON THE MERCHANT
MARINE**

OF THE

**COMMITTEE ON NATIONAL SECURITY
HOUSE OF REPRESENTATIVES**

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

HEARING HELD

MARCH 28 AND APRIL 6, 1995



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON : 1996

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SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE

HERBERT H. BATEMAN, Virginia, *Chairman*

RANDY "DUKE" CUNNINGHAM, California	GENE TAYLOR, Mississippi
HUNTER DUNCAN, California	OWEN PICKETT, Virginia
CURT WELDON, Pennsylvania	NEIL ABERCROMBIE, Hawaii
JIM SAXTON, New Jersey	JANE HARMAN, California
JOE SCARBOROUGH, Florida	PATRICK J. KENNEDY, Rhode Island
JAMES B. LONGLEY, JR., Maine	WILLIAM J. JEFFERSON, Louisiana
TILLIE K. FOWLER, Florida	

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ANNUAL AUTHORIZATION OF THE PANAMA CANAL COMMISSION AND THE ANNUAL AUTHORIZATION FOR THE UNITED STATES MARITIME ADMINISTRATION

HOUSE OF REPRESENTATIVES,
COMMITTEE ON NATIONAL SECURITY,
SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE,
Washington, DC, Tuesday, March 28, 1995.

The subcommittee met, pursuant to call, at 2 p.m., in room 2216, Rayburn House Office Building, Hon. Herbert H. Bateman (chairman of the panel) presiding.

OPENING STATEMENT OF HON. HERBERT H. BATEMAN, A REPRESENTATIVE FROM VIRGINIA, CHAIRMAN, SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE

Mr. BATEMAN. The panel will come to order and we will proceed with our hearing. In today's hearing, we cover two very important topics, the annual authorization of the Panama Canal Commission and the annual authorization for the U.S. Maritime Administration.

As many of you know, the National Security Committee assumed responsibility over these two agencies with the House rules change on January 4, 1995. As you may be aware, we have a distinguished list of panelists who will be here today. I would like to thank each of them for appearing before us.

I would first want to extend a very personal welcome to the Honorable Gilberto Guardia, the Administrator of the Panama Canal Commission and of course to Secretary Joe R. Reeder who is Chairman of the Board of Directors of the Commission.

Mr. Guardia, I trust that your visit to the Nation's Capital will be a very pleasant and a satisfactory one. I don't anticipate anything will happen this afternoon that would make it less than pleasant.

The canal, the future of the canal and the relations of the United States with Panama are timely and important issues. It was for that reason that I asked the key representatives from the State Department and the Pentagon to appear before the panel today.

The issues raised in the written testimony which I have reviewed offer this panel an excellent starting point to begin what I expect will be a lengthy examination. I believe membership interest in the subject will be high.

Finally, I would like to welcome Admiral Herberger, the Administrator of the Maritime Administration and Admiral Quast, the commander of the Military Sealift Command.

The organization of neither would exist without the other. It is for that reason that I have asked them if they would appear to-

gether. Maritime reform is something that has occupied the Congress for several years. I hope we will have more than just hearings to show for our efforts at the end of this Congress.

I will continue this inquiry on the Maritime Security Program on Thursday of next week, April 6, at which time we will hear from representatives of the affected industries within the maritime community.

I would now call on the ranking member of the panel, the Honorable Gene Taylor of Mississippi for any remarks he may choose to make.

**STATEMENT OF HON. GENE TAYLOR, A REPRESENTATIVE
FROM MISSISSIPPI, RANKING MINORITY MEMBER, SPECIAL
OVERSIGHT PANEL ON THE MERCHANT MARINE**

Mr. TAYLOR. Mr. Chairman, if you don't mind, I will submit my opening statement for the record. I also want to thank our guests who traveled a long way to be with us today. We look forward to hearing from them.

I would hope that at some point during today's hearings with regard to the Panama Canal we could discuss, or at least begin to talk about, the possibility of continued United States military presence in Panama should it be the wishes of the Panamanian people and this Congress to do so.

I thank you very much. I will just submit my remarks for the record.

[The prepared statement of Mr. Taylor follows:]

Statment of Congressman Gene Taylor
Ranking Member, Special Oversight
Panel on the Merchant Marine
Hearing
Tuesday, March 28, 1995

I WOULD LIKE TO THANK OUR CHAIRMAN, HERBERT BATEMAN, MY FELLOW MEMBERS OF THE PANEL, AND OUR DISTINGUISHED WITNESSES FOR PARTICIPATING IN TODAY'S HEARING ON THE FY 96 AUTHORIZATIONS FOR THE PANAMA CANAL COMMISSION AND THE MARITIME ADMINISTRATION.

I AM EXTREMELY PROUD TO HAVE THE OPPORTUNITY TO SERVE ALONG SIDE CHAIRMAN BATEMAN ON THIS PANEL. MR. BATEMAN HAS BEEN A STRONG SUPPORTER OF THE U.S. MARITIME INDUSTRY AND HAS DISTINGUISHED HIMSELF IN CONGRESS AS A CHAMPION OF OUR NATION'S SHIPBUILDING INDUSTRY. I LOOK FORWARD TO SERVING WITH YOU, MR. CHAIRMAN, AS WELL AS THE OTHER MEMBERS OF THE PANEL WHO I'M SURE THAT I'LL AGREE WITH ON 99 PERCENT OF THE ISSUES THAT WE ADDRESS.

IT IS MY UNDERSTANDING THAT WE WILL BE ADDRESSING THE FISCAL YEAR 1996 BUDGET REQUEST FOR THE PANAMA CANAL COMMISSION FIRST. I AM PLEASED THAT ONE OF THE ISSUES THAT WE WILL DISCUSS AT TODAY'S HEARING WILL BE THE MATTER OF U.S. MILITARY PRESENCE IN PANAMA AFTER DECEMBER 31, 1999.

DURING THE MARAD PORTION THIS HEARING, I WISH TO EXPRESS MY STRONG SUPPORT TO THE TITLE XI LOAN GUARANTEE PROGRAM. TITLE XI IS OUR NATION'S ONLY SHIPYARD PROGRAM WHICH IS MODESTLY FUNDED (\$85 MILLION LEFT IN UNOBLIGATED APPROPRIATED FUNDS). OUR FOREIGN COMPETITORS CURRENTLY HAVE SUBSIDY PROGRAMS THAT TOTAL \$8 BILLION.

I WILL DISCUSS THESE ISSUES IN GREATER DEPTH AT THE PROPER TIME LATER ON. AGAIN, THANK YOU MR. CHAIRMAN. I YIELD BACK THE BALANCE OF MY TIME.

Mr. BATEMAN. It will be accepted for the record.

At this point, it is my pleasure to welcome and to further thank the Chairman of the Panama Canal Commission, the Honorable Joe Reeder, who is the Under Secretary of the Army. Thank you so much for being with us.

Mr. REEDER. Thank you, Mr. Chairman.

Mr. BATEMAN. You may proceed.

STATEMENT OF HON. JOE R. REEDER, CHAIRMAN, BOARD OF DIRECTORS, PANAMA CANAL COMMISSION; ACCOMPANIED BY MICHAEL RHODE, JR., ASSISTANT TO THE CHAIRMAN AND SECRETARY, PANAMA CANAL COMMISSION

Mr. REEDER. Thank you, Mr. Chairman.

Both Mr. Guardia, the Administrator, and I look forward to presenting our testimony to you and to the panel today. Seated with us on my right is the Secretary of the Commission, Mr. Michael Rhode, Jr.

On Mr. Guardia's left, the Commission's Chief Financial Officer, Mr. Norbert Kraegel. I would like to begin, Mr. Chairman, by extending a warm welcome to you and to the other members of the panel, Congressmen Longley and Taylor. We look very much forward to your visit in late April.

I hope to be down there and overlap with you at least 1 day on that when we have our quarterly board meeting. We also look forward to a productive relationship with you, your staff, and the panel as the Commission continues to carry out its two most important missions. First, the safe efficient operation of the canal. Second, its smooth and orderly transfer to the Government of Panama at noon, December 31, 1999.

The Panama Canal Commission or PCC, continues its preparation of transfer of the canal to Panamanian control in less than 5 years. While Mr. Guardia will address transition issues and the progress of the Republic of Panama, I would like to simply highlight examples of significant progress on this front.

Of course our immediate purpose in coming before you is to present our plans and programs for the next fiscal year and to help secure our regular authority to operate during that fiscal year. There is another piece of proposed legislation I would like to briefly touch on which has a longer focus.

This proposed legislation entitled "The Panama Canal Amendments Act of 1995" has been years in development and seeks to make changes we believe will facilitate a successful and seamless transfer of the canal in 1999.

Of course, the United States and almost all trading nations will continue to have a strong interest in a healthy efficient Panama Canal operation. The proposal was transmitted to the House of Representatives on March 9 and referred to the National Security Committee. We hope that it will be introduced shortly.

The main features of the proposal would be to convert the Commission from a revolving fund agency to a wholly owned Government corporation, and to revamp the Board of Directors to a more dynamic, empowered corporate form.

The reason for the legislation is to have the Commission in a form advantageous for Panama to retain. This would decrease the

turbulence and uncertainty which could be caused by dramatic changes in the agency right at the juncture or point of transfer.

The new constitutional title enacted by the Republic of Panama provides authority for Panama to create a Panama Canal agency which is semiautonomous and has private sector features. We see this as a good development and would like to ensure that we have an efficiently operating corporation in place well before December 31, 1999, which could continue operating under Panamanian law.

The legislation has strong support from the Departments of Defense and State, from the Commission itself, the Panama Canal Commission, and of course from the White House. I believe it important for the long-term interest of the canal, as well as those of the United States for this legislation to be enacted in this session of Congress.

We will appreciate your consideration in support of this, Mr. Chairman. In 1994, the Panama Canal completed its 15th year of successful operation under the treaty and celebrated its 80th anniversary of service to world shipping.

A key element of the canal's optimal service to customers is the high priority we give to the waterway's maintenance and modernization programs. To keep pace with the ever changing demands of world trade, the Commission has invested over \$1.5 billion since 1979 to maintain, improve, and modernize the canal facilities.

The canal also operates efficiently as a result of its strong emphasis on employee training. Employee programs are designed to attract, and equally important if not more important, to retain a top quality labor force in the local Panamanian market, and to increase the number of Panamanians in key management and professional positions.

The Panamanians now comprise in excess of 89 percent of the canal's permanent work force. More than half of our professionals and managers now are Panamanians.

In Washington's current environment of downsizing and streamlining under the guidance of Vice President Gore's National Performance Review, I am also pleased to report that many of the NPR objectives are a top priority for the canal organization.

To survive in the marketplace, the Commission must provide safe, efficient and cost competitive service to achieve a high level of customer satisfaction and maintain the loyalty and business of its customers.

As such, the Commission, for decades, has strived to achieve the cost reduction, streamlining and customer service goals which underpin the NPR. Fiscal year 1994 was a turn around year for the Commission as Mr. Guardia's testimony will explain.

Because of the canal's strong performance in 1994, the Commission made contingency profit payment of \$1.1 million to the Republic of Panama in accordance with the treaty of 1977. Both canal traffic and toll revenue continue to perform strongly in this fiscal year.

We believe additional growth will continue in fiscal year 1996. Mr. Guardia will address the Commission's fiscal year 1996 budget in some detail. Let me add that programs he covers are essential to ensure continued customer satisfaction, proper systems mainte-

nance, a break even budget, and detailed transition planning and execution. They are consistent with the President's program.

In closing, I would like to recognize the loyalty and commitment of the entire employee work force. This work force constitutes the heart of this great 80-year-old enterprise. It continues to perform as professionals in providing quality transit service to vessels of all nations.

Their commitment to teamwork remains the most important asset to the future and success of the canal. Thank you, Mr. Chairman.

[The prepared statement of Mr. Reeder follows:]

**FISCAL YEAR 1996
BUDGET PROGRAMS
STATEMENT OF THE CHAIRMAN
OF THE BOARD OF DIRECTORS
PANAMA CANAL COMMISSION**

BEFORE THE

**NATIONAL SECURITY COMMITTEE
SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE
U.S. HOUSE OF REPRESENTATIVES**

**MARCH 28, 1995
2:00 P.M. RAYBURN HOUSE OFFICE BUILDING**

INTRODUCTION

MR. CHAIRMAN, MEMBERS OF THE MERCHANT MARINE PANEL, I AM JOE R. REEDER. I SERVE AS CHAIRMAN OF THE BOARD OF THE PANAMA CANAL COMMISSION, AND AS UNDER SECRETARY OF THE ARMY. I HAVE BEEN A BOARD MEMBER SINCE JANUARY, 1994 AND WAS ELECTED CHAIRMAN BY MY FELLOW BOARD MEMBERS LAST OCTOBER. MR. GILBERTO GUARDIA, THE COMMISSION'S ADMINISTRATOR, IS ALSO SUBMITTING TESTIMONY TO THE COMMITTEE. WE ARE ABLY ASSISTED BY MR. MICHAEL RHODE, SECRETARY OF THE COMMISSION, AND MR. NORBERT KRAEGEL, THE COMMISSION'S CHIEF FINANCIAL OFFICER.

I WOULD LIKE TO EXTEND A WARM WELCOME TO YOU, MR. CHAIRMAN, MR. VICE-CHAIRMAN, AND THE MEMBERS OF THIS PANEL. WE LOOK FORWARD TO A PRODUCTIVE RELATIONSHIP WITH YOU AND YOUR STAFF AS THE COMMISSION CONTINUES TO CARRY OUT ITS TWO MOST IMPORTANT MISSIONS: THE SAFE, EFFICIENT OPERATION OF THE CANAL, AND ITS SMOOTH AND ORDERLY

TRANSFER TO THE GOVERNMENT OF PANAMA AT NOON, DECEMBER 31, 1999, AS REQUIRED BY THE PANAMA CANAL TREATY.

TRANSITION ISSUES

THE PANAMA CANAL COMMISSION CONTINUES ITS PREPARATION TO TRANSFER THE CANAL TO PANAMANIAN CONTROL IN LESS THAN FIVE YEARS. THE ADMINISTRATOR WILL ADDRESS TRANSITION ISSUES AND THE PROGRESS OF THE REPUBLIC OF PANAMA. I WOULD LIKE TO SIMPLY HIGHLIGHT EXAMPLES OF SIGNIFICANT PROGRESS ON THIS FRONT.

OF COURSE, OUR IMMEDIATE PURPOSE IN COMING BEFORE YOU IS TO PRESENT OUR PLANS AND PROGRAMS FOR THE NEXT FISCAL YEAR, AND TO HELP SECURE OUR REGULAR AUTHORITY TO OPERATE IN THAT NEXT FISCAL YEAR. BUT THERE IS ANOTHER PIECE OF PROPOSED LEGISLATION I WOULD LIKE TO BRIEFLY TOUCH ON WHICH HAS A LONGER FOCUS.

THIS PROPOSED LEGISLATION, ENTITLED "THE PANAMA CANAL AMENDMENTS ACT OF 1995," HAS BEEN YEARS IN DEVELOPMENT AND SEEKS TO MAKE CHANGES WHICH WE BELIEVE WILL FACILITATE A SUCCESSFUL AND SEAMLESS TRANSFER OF THE CANAL IN 1999. OF COURSE, THE U.S. AND ALMOST ALL TRADING NATIONS WILL CONTINUE TO HAVE A STRONG INTEREST IN A HEALTHY, EFFICIENT PANAMA CANAL OPERATION.

THIS LEGISLATION WAS DEVELOPED TO COMPLY WITH A PROVISION IN OUR 1993 AUTHORIZATION BILL, WHICH MANDATED A STUDY TO DETERMINE WHAT CHANGES, IF ANY, TO THE COMMISSION WOULD BETTER FACILITATE THE SMOOTH TRANSFER TO PANAMANIAN CONTROL. THE LEGISLATION HAS STRONG SUPPORT FROM THE DEPARTMENTS OF DEFENSE AND STATE, THE PANAMA CANAL COMMISSION, AND OF COURSE THE WHITE HOUSE.

THE PROPOSAL WAS TRANSMITTED TO THE HOUSE OF REPRESENTATIVES ON MARCH 9, AND REFERRED TO THE NATIONAL SECURITY COMMITTEE. WE HOPE THAT IT WILL BE INTRODUCED SHORTLY. THE MAIN FEATURES OF THE PROPOSAL WOULD BE TO

CONVERT THE COMMISSION FROM A REVOLVING FUND AGENCY TO A WHOLLY-OWNED GOVERNMENT CORPORATION, AND TO REVAMP THE BOARD OF DIRECTORS TO A MORE DYNAMIC, EMPOWERED CORPORATE FORM.

THE REASON FOR THE LEGISLATION IS TO HAVE THE COMMISSION IN A FORM ADVANTAGEOUS FOR PANAMA TO RETAIN. THIS WOULD DECREASE THE TURBULENCE AND UNCERTAINTY WHICH COULD BE CAUSED BY DRAMATIC CHANGES IN THE AGENCY RIGHT AT THE POINT OF TRANSFER.

THE NEW CONSTITUTIONAL TITLE ENACTED BY THE REPUBLIC OF PANAMA PROVIDES THE AUTHORITY FOR PANAMA TO CREATE A PANAMA CANAL AGENCY WHICH IS SEMI-AUTONOMOUS AND HAS PRIVATE-SECTOR FEATURES. WE SEE THIS AS A GOOD DEVELOPMENT, AND WOULD LIKE TO ENSURE THAT WE HAVE AN EFFICIENTLY OPERATING CORPORATION IN PLACE WELL BEFORE DECEMBER 31, 1999, WHICH COULD CONTINUE OPERATING UNDER PANAMANIAN LAW.

I BELIEVE IT IS IMPORTANT FOR THE LONG-TERM INTERESTS OF THE CANAL, AS WELL AS THOSE OF THE UNITED STATES, FOR THIS LEGISLATION TO BE ENACTED IN THIS SESSION OF CONGRESS, AND WE WILL APPRECIATE YOUR CONSIDERATION AND SUPPORT OF IT.

I KNOW THAT MR. GUARDIA WILL ADDRESS THE PANEL ON THE RECENT SIGNIFICANT STEPS PANAMA HAS TAKEN IN ITS TRANSITION PLANNING, SO I WILL LEAVE THAT SUBJECT IN HIS VERY CAPABLE HANDS.

BOARD ACTIVITIES

AMONG BOARD ACTIVITIES IN 1994, TWO NEW U.S. BOARD MEMBERS, MR. ALBERT NAHMAD AND MR. CLIFFORD O'HARA, WERE CONFIRMED BY THE SENATE AND APPOINTED BY THE PRESIDENT. BOTH ATTENDED THEIR FIRST BOARD MEETING LAST OCTOBER. THEY REPLACE MR. ROBERT MCMILLAN, WHO BECAME A MEMBER OF THE BOARD IN 1989, AND MR. WILLIAM CARL, WHO SERVED ON THE BOARD FOR TWO YEARS. HAVING SERVED AS A CHARTER BOARD MEMBER FROM 1980 TO 1982, MR. O'HARA IS FAMILIAR WITH THE

COMMISSION OPERATION, AND HE IS AN EXPERT ON SHIPPING AND PORTS. AS CHIEF EXECUTIVE OFFICER OF A SUCCESSFUL NATIONWIDE MANUFACTURING DISTRIBUTORSHIP, MR. NAHMAD BRINGS TO THE BOARD A WEALTH OF VALUABLE BUSINESS EXPERTISE.

THE PANAMANIAN PRESIDENT HAS NOMINATED FOUR NEW MEMBERS TO REPLACE THE FOUR CURRENT PANAMANIAN BOARD MEMBERS, ALL OF WHOM HAVE PROVIDED INVALUABLE SERVICE TO THE BOARD FOR FOUR TO ELEVEN YEARS. THESE NOMINEES, WHO ARE AWAITING U.S. PRESIDENTIAL APPOINTMENT, ATTENDED THE COMMISSION'S RECENT JANUARY MEETING AS OBSERVERS. THEIR ATTENDANCE PROVIDED A FAVORABLE OVERLAP OF EXPERIENCE WITH THE CURRENT PANAMANIAN REPRESENTATIVES. WE EXPECT THEM TO SHARE THEIR PREDECESSORS' DEDICATION TO ENSURING A SUCCESSFUL TRANSITION AND ASSUMING CONTROL OF THE CANAL ENTERPRISE, WHICH IS WIDELY REGARDED AS ONE OF THE MOST IMPORTANT ECONOMIC ACTIVITIES IN THE REPUBLIC OF PANAMA.

LAST AUGUST, THE BOARD APPROVED AND FORWARDED TO PRESIDENT CLINTON A RECOMMENDATION TO APPROVE THE ADOPTION OF A WORLDWIDE STANDARD OF TONNAGE MEASUREMENT FOR THE ASSESSMENT OF TOLLS. THE PANAMA CANAL UNIVERSAL MEASUREMENT SYSTEM WAS APPROVED BY THE PRESIDENT, AND TOOK EFFECT ON OCTOBER 1. THE SYSTEM IS WORKING VERY SMOOTHLY. CANAL CUSTOMERS WILL BENEFIT FROM THE MORE STREAMLINED MEASUREMENT PROCESS USING COMPUTER GENERATED SKIN-TO-SKIN MEASUREMENTS, THUS REMOVING SUBJECTIVE JUDGMENT FROM THE TONNAGE CALCULATION.

OPERATING ENVIRONMENT

IN 1994, THE PANAMA CANAL COMPLETED ITS 15TH YEAR OF SUCCESSFUL OPERATION UNDER THE PANAMA CANAL TREATY AND CELEBRATED ITS 80TH ANNIVERSARY OF SERVICE TO WORLD SHIPPING. THE BEST EVIDENCE OF THE CANAL'S EXCELLENT OPERATING CONDITION LIES IN ITS TRAFFIC LEVELS, WHICH IN 1994

REVERSED A TWO-YEAR DECLINE IN BOTH COMMERCIAL CARGO AND PANAMA CANAL NET TONS TRANSITING THE CANAL.

A KEY ELEMENT OF THE CANAL'S OPTIMAL SERVICE TO CUSTOMERS IS THE HIGH PRIORITY WE GIVE TO THE WATERWAY'S MAINTENANCE AND MODERNIZATION PROGRAMS. TO KEEP PACE WITH THE EVER-CHANGING DEMANDS OF WORLD TRADE, THE COMMISSION HAS INVESTED OVER \$1.5 BILLION DOLLARS SINCE 1979 TO MAINTAIN, IMPROVE AND MODERNIZE THE CANAL.

THE CANAL ALSO OPERATES EFFICIENTLY AS A RESULT OF ITS STRONG EMPHASIS ON EMPLOYEE TRAINING. BECAUSE A PRIMARY COMMISSION MISSION IS TO ENSURE THE SMOOTH AND ORDERLY TRANSFER OF THE CANAL TO PANAMA, EMPLOYEE PROGRAMS ARE DESIGNED TO ATTRACT AND RETAIN A TOP QUALITY LABOR FORCE FROM THE LOCAL MARKET, AS WELL AS INCREASE THE NUMBER OF PANAMANIAN IN KEY MANAGEMENT AND PROFESSIONAL POSITIONS. PANAMANIAN NOW COMPRISE OVER 89 PERCENT OF THE CANAL'S PERMANENT WORK FORCE OF OVER 7,400 EMPLOYEES.

MORE THAN HALF OF OUR PROFESSIONALS AND MANAGERS NOW ARE PANAMANIAN.

IN WASHINGTON'S CURRENT ENVIRONMENT OF DOWNSIZING AND STREAMLINING UNDER THE GUIDANCE OF VICE PRESIDENT GORE'S NATIONAL PERFORMANCE REVIEW, I AM PLEASED TO REPORT THAT MANY OF THE NPR OBJECTIVES HAVE LONG BEEN A WAY OF LIFE FOR THE CANAL ORGANIZATION. WHERE NEW IDEAS PRESENT AN OPPORTUNITY FOR GREATER IMPROVEMENT, WE PURSUE THEM VIGOROUSLY. THE CANAL OPERATES AS A COMMERCIAL ENTERPRISE WITH NO APPROPRIATED FUNDS WHATSOEVER FROM THE U.S. TREASURY. IN ORDER TO SURVIVE IN THE MARKETPLACE, THE COMMISSION MUST PROVIDE SAFE, EFFICIENT AND COST-COMPETITIVE SERVICE TO ACHIEVE A HIGH LEVEL OF CUSTOMER SATISFACTION AND MAINTAIN THE LOYALTY AND BUSINESS OF ITS CUSTOMERS. AS SUCH, THE COMMISSION IS ALWAYS STRIVING TO ACHIEVE THE COST REDUCTION, STREAMLINING, AND CUSTOMER SERVICE GOALS SOUGHT BY NPR.

BUDGET PROGRAMS

FISCAL YEAR 1994 WAS A TURN-AROUND YEAR FOR THE COMMISSION. REVERSING THE DECLINING TRAFFIC TREND OF THE LAST TWO YEARS, CANAL TRAFFIC AND TOLLS REVENUE PERFORMED STRONGLY DURING 1994, WITH SOME MAJOR ELEMENTS OF TRAFFIC REACHING RECORD LEVELS. TRANSITS BY PANAMAX VESSELS -- THOSE WITH BEAMS OF 100 FEET AND OVER -- INCREASED 7 PERCENT OVER THE PRIOR YEAR, AND OCEANGOING COMMERCIAL CARGO AND PANAMA CANAL NET TONNAGE CLIMBED TO THE HIGHEST LEVELS SINCE 1982. AS MR. GUARDIA'S TESTIMONY WILL EXPLAIN, BECAUSE OF THIS UPTURN, THE COMMISSION MADE A CONTINGENCY PROFIT PAYMENT OF \$1.1 MILLION DOLLARS TO THE REPUBLIC OF PANAMA IN ACCORDANCE WITH THE PANAMA CANAL TREATY OF 1977.

THE IMPROVED ECONOMIC PERFORMANCE IN VARIOUS PARTS OF THE WORLD HAVE FAVORABLY AFFECTED CANAL TRADE IN THIS FISCAL YEAR. BOTH CANAL TRAFFIC AND TOLLS REVENUE CONTINUE TO PERFORM STRONGLY, SUPPORTING THE EXPECTATION THAT

ADDITIONAL GROWTH WILL BE EXPERIENCED IN THE REMAINDER OF THE YEAR, AND WILL CONTINUE IN FISCAL YEAR 1996.

MR. CHAIRMAN, MR. GUARDIA'S STATEMENT ADDRESSES THE COMMISSION'S FISCAL YEAR 1996 BUDGET IN SOME DETAIL. LET ME ADD THAT THE PROGRAMS COVERED BY MR. GUARDIA ARE ESSENTIAL TO ENSURE CONTINUED CUSTOMER SATISFACTION, PROPER SYSTEMS MAINTENANCE, A BREAK-EVEN BUDGET, AND DETAILED TRANSITION PLANNING AND EXECUTION. THEY ARE CONSISTENT WITH THE PRESIDENT'S PROGRAM.

RECOGNITION OF CANAL EMPLOYEES

IN CLOSING, I WOULD LIKE TO EXPRESS THE APPRECIATION OF THE BOARD MEMBERS FOR THE LOYALTY AND COMMITMENT OF ALL PANAMA CANAL COMMISSION EMPLOYEES. OUR EMPLOYEES ARE THE HEART OF THIS GREAT ENTERPRISE, AND CONTINUE TO PERFORM AS PROFESSIONALS IN PROVIDING QUALITY TRANSIT SERVICE TO VESSELS OF ALL NATIONS. THEIR COMMITMENT TO

TEAM WORK REMAINS THE MOST IMPORTANT ASSET TO THE FUTURE
SUCCESS OF THE CANAL.

Mr. BATEMAN. Thank you, Secretary Reeder.

Now, it is our pleasure to invite Mr. Guardia to present his testimony.

Mr. GUARDIA. Thank you, Mr. Chairman. With your permission, I will summarize my testimony and submit it for the record.

Mr. BATEMAN. All right. It will be made a part of the record in full. You may proceed as you choose.

STATEMENT OF GILBERTO F. GUARDIA, ADMINISTRATOR, PANAMA CANAL COMMISSION

Mr. GUARDIA. I would like to take this opportunity to express my sincere appreciation to the members of this panel for the support and assistance that it has provided the Panama Canal Commission in the past. I look forward to the continuation of this productive relationship under your leadership.

As background for the review of our fiscal year 1996 budget programs, I will make just a few comments on our operating results for 1994, the outlook for 1995, and our budget for 1996.

Canal traffic performed strongly during 1994, reversing a 2-year declining trend. Commercial cargo transit in the waterways in the Panama Canal net tonnage was the highest since the 1982 historical peak.

These gains reflect the economic recovery in the United States, sustained economic growth of the Pacific rim economies, and the good economic performance of certain South American countries.

Toll revenues of \$419 million were up 4.6 percent from 1993. Total operating revenues for the year were \$548 million. Operating expenses were \$546 million or about 4 percent over 1993. The bottom line had net revenues of \$1.7 million, with \$600,000 applied to recover a loss carried over and \$1.1 million paid to the Government of Panama in accordance with the requirements of the Panama Canal Treaty.

Additional growth in traffic is anticipated in 1995 as the U.S. economy continues to grow and trade recovery occurs worldwide. Latin American trade with the United States and Europe is expected to continue expanding as economic reform in the nations of this region stimulate trade and investment.

Toll revenues are estimated at \$428 million, an increase of 2 percent from the high levels of 1994. Total operating revenues are forecast at \$561 million. Operating expenses are also budgeted at \$561 million; an increase of 2.7 percent. A break-even operation is forecast for all of 1995.

Our budget for 1996 anticipates that traffic and toll revenue will continue to grow modestly as the United States economy expands beyond the first half of the year and the European and Japanese economic recoveries strengthen.

Toll revenues at existing toll rates is forecast at \$435 million; an increase of 1.6 percent. Total revenues are estimated at \$571 million. Operating costs in 1996 are estimated at \$571 million as well; an increase of only 1.8 percent over 1995.

The break-even operation is budgeted for 1996, recovering all costs of operations and the funds for its Capital Improvement Program. The capital program for 1996 is \$40 million and will be used

principally for essential transit facilities and equipment, to improve operational safety and efficiency, and to modernize the canal.

A major continuing project is widening and straightening of the Gaillard Cut. We have budgeted \$10 million for this program, bringing the total for 1991 through 1996 to \$41 million. The Commission is also replacing its 80-year-old heavy lift crane, Hercules, with a Titan, a larger high quality crane.

The Titan was recently accessed at the Long Beach Naval Station and transferred to the Commission. We plan to spend about \$12 million for modifications and reconditioning.

Last year, I reported on a number of important initiatives underway in Panama dealing with the planning and preparation of the transfer of the canal on December 31, 1999. I am pleased to report that the new—moved quickly to gain the required second legislative approval of the constitutional amendment, providing for an autonomous entity to administer and operate the canal in the year 2000 and beyond.

Gorman efforts are now underway to draft an organic law implementing the constitutional amendment. I fully expect that I and other Commission officials will be asked to participate as advisers or resource personnel in Panama's efforts to develop the comprehensive package of laws to administer post-1999 canal operations.

President Perez Balladares inaugurated a Panama Transition Commission on January 24, 1995, to coordinate and oversee for Panama all matters relating to the transfer of the canal enterprise. This new Commission essentially replaces a Presidential Commission of Civilian Advisers established during the Endara administration. The Commission includes the four new Panamanian member designates to the Panama Canal Commission Board of Directors, the three Panamanian members of the treaty-based Consultative Committee, plus the Director General of Canal Affairs and the Director of the Panamanian Treaty Affairs Executive Bureau.

I plan to play an active advisory role in the Commission's activities and, in fact, we have already started this relationship.

In closing, I would like to highlight certain actions and activities to prepare for the year 2000. We are investing approximately \$125 million a year in maintaining, modernizing, and improving the canal.

We are striving to maintain a high degree of professionalism and morale among our employees. Panamanian citizens now comprise over 89 percent of the Commission's work force, with increasing involvement at all management levels.

I continue to be actively involved along with senior members of my staff in presenting especially designed briefings on canal operations to a variety of Panamanian Government task forces, maritime conferences, trade conventions, and local business organizations in Panama.

The thrust of these presentations has been to identify and highlight the policies, systems, and functions that are currently necessary for the successful management and administration of the Panama Canal. Lastly, Mr. Chairman, I wish to underscore the comments made by the Chairman regarding the proposed legisla-

tion to, among other things, convert the Panama Canal Commission to a wholly owned Government corporation.

It is important to the future of the canal and to both the United States and Panama that we begin the conversion as soon as possible. I ask your support in this endeavor.

Mr. Chairman, that concludes my statement. I will be pleased to answer any questions together with Mr. Reeder that you may have. Thank you very much.

[The prepared statement of Mr. Guardia follows:]

MR. GILBERTO GUARDIA
ADMINISTRATOR OF THE PANAMA CANAL COMMISSION

Mr. Gilberto Guardia was appointed Administrator of the Panama Canal Commission on September 20, 1990, by the President of the United States. He holds the special distinction of being the first Panamanian citizen appointed to the top position in the Canal agency. As the Commission Administrator, Mr. Guardia is responsible for the management, operation and maintenance of the Panama Canal and preparing the Canal for its orderly transfer to full Panamanian control on December 31, 1999.

Mr. Guardia was born in Panama City, Republic of Panama on February 13, 1930. He graduated from the University of Santa Clara in California in 1950 with a degree in civil engineering. Following his graduation he briefly worked as a civil engineer with the Panama Canal Company, which gave him the opportunity to become familiar with the organization's wide range of engineering activities. Mr. Guardia is a well recognized and respected engineer in Panama, previously heading the prestigious architectural, engineering and construction firm of Diaz y Guardia, S.A. Under his leadership, the company designed and constructed schools, homes and commercial buildings primarily in Panama City and the Canal area. That firm is also credited with projects such as the Bayano Cement Factory, the Banco Exterior building and the Bahá'í Temple, which are all spectacular landmarks in Panama.

The Panamanian Society of Professional Engineers and Architects has honored Mr. Guardia with the Florencio Icaza Award, which recognizes excellence among professional engineers and architects in Panama. Additionally, he has been very active over the years in various civic and professional organizations in Panama. Mr. Guardia has served on the boards of numerous organizations including the Banque Nationale de Paris in Panama; Panama Construction Chamber; World Business Council in Washington, D.C.; Panama's National Association for Conservation of Nature and the Panama South Chapter of the Rotary Club. He has been a long-time member and past president of the Panama Business Executives Association and was named "Executive of the Year" in 1992 by that organization.

Since his appointment as Administrator of the Panama Canal Commission, Mr. Guardia has worked diligently to ensure continued high quality transit service to Canal customers. Among the major Canal improvement programs undertaken during his tenure are the widening and straightening of Gaillard Cut, widening of the Canal's entrance channels, major locks overhauls and associated refurbishment work, completion of a marine foam fire protection system at Miraflores Locks and work on a similar system at Pedro Miguel Locks, installation of a new prototype flat fendering system at all locks, construction of a vessel signal station for improved monitoring of vessel traffic at the Atlantic entrance, and installation of a shiphandling simulator to improve in-house training of Canal pilots. In fulfillment of treaty responsibilities, Mr. Guardia is committed to ensuring the smooth transfer of the Canal to Panamanian control at the end of the century.

Revised by the Office of Executive Planning, June 21, 1994

**FISCAL YEAR 1996
BUDGET PROGRAMS**



**STATEMENT OF THE
ADMINISTRATOR
PANAMA CANAL COMMISSION**

BEFORE THE

NATIONAL SECURITY COMMITTEE

**SPECIAL OVERSIGHT PANEL
ON THE MERCHANT MARINE**

U.S. HOUSE OF REPRESENTATIVES

**March 28, 1995
2:00 p.m.
Rayburn House Office Building**

INTRODUCTION

MR. CHAIRMAN, MEMBERS OF THE PANEL, I AM GILBERTO GUARDIA, ADMINISTRATOR OF THE PANAMA CANAL COMMISSION. I AM PLEASED TO APPEAR BEFORE YOU TODAY TO PRESENT THE FISCAL YEAR 1996 BUDGET PROGRAMS OF THE PANAMA CANAL COMMISSION, THE UNITED STATES AGENCY RESPONSIBLE FOR THE MANAGEMENT AND OPERATION OF THE PANAMA CANAL.

I WOULD LIKE TO TAKE THIS OPPORTUNITY TO EXPRESS MY SINCERE APPRECIATION TO THE PANEL MEMBERS FOR THE SUPPORT AND ASSISTANCE THEY HAVE PROVIDED THE PANAMA CANAL COMMISSION IN THE RECENT YEARS. MR. CHAIRMAN, I LOOK FORWARD TO A CONTINUATION OF THIS HARMONIOUS AND PRODUCTIVE RELATIONSHIP UNDER YOUR LEADERSHIP.

AS BACKGROUND FOR THE REVIEW OF OUR FISCAL YEAR 1996 BUDGET PROGRAMS, I WILL COMMENT FIRST ON THE COMMISSION'S OPERATING RESULTS FOR FISCAL YEAR 1994 AND OUR CURRENT OUTLOOK FOR FISCAL YEAR 1995.

OPERATING RESULTS FOR FISCAL YEAR 1994

CANAL TRAFFIC AND TOLLS REVENUE PERFORMED STRONGLY DURING FISCAL YEAR 1994, REVERSING A TWO-YEAR DECLINING TREND. THE 171 MILLION LONG TONS OF OCEANGOING COMMERCIAL CARGO REGISTERED IN FISCAL YEAR 1994 MARKED THE HIGHEST VOLUME OF CARGO SINCE 1982. PANAMA CANAL NET TONNAGE ALSO ROSE SUBSTANTIALLY DURING THE YEAR TO 196 MILLION TONS, RECORDING THE HIGHEST TONNAGE AFTER THE 1982 HISTORICAL PEAK OF 204 MILLION TONS.

A TOTAL OF 12,478 OCEANGOING TRANSITS, OR AN AVERAGE OF 34.2 DAILY, WERE REGISTERED AT THE WATERWAY DURING THE YEAR, INCREASING 1.8 PERCENT FROM THE 12,257 TRANSITS, OR 33.6 DAILY, RECORDED IN FISCAL YEAR 1993. AVERAGE SHIP SIZE CONTINUED UPWARD IN 1994, WITH TRANSITS BY VESSELS HAVING BEAMS OF 30.5 METERS (100 FEET) AND OVER, BREAKING THE PREVIOUS YEAR RECORD.

THE SIGNIFICANT IMPROVEMENTS IN TRAFFIC WERE CAUSED PRIMARILY BY THE ECONOMIC RECOVERY IN THE UNITED STATES, SUSTAINED ECONOMIC GROWTH OF THE PACIFIC RIM NEWLY INDUSTRIALIZED ECONOMIES (NIES), AND THE GOOD ECONOMIC PERFORMANCE OF CERTAIN SOUTH AMERICAN COUNTRIES.

THE UPTURN WAS DRIVEN BY THE STRONG PERFORMANCE OF A NUMBER OF KEY COMMODITIES, INCLUDING MANUFACTURES OF IRON AND STEEL, MISCELLANEOUS MINERALS, WHEAT, PHOSPHATE, CRUDE OIL, CONTAINERIZED CARGO, COAL, REFRIGERATED SHIPMENTS, AND AUTOMOBILE TONNAGE. THESE INCREASES OFFSET DECLINES IN CORN, SOYBEAN, AND LUMBER TONNAGE.

THE RISE IN BOTH TRANSIT NUMBERS AND AVERAGE SHIP SIZE INCREASED TOTAL P.C. NET TONNAGE BY 4.1 PERCENT, TO 195.6 MILLION TONS. AS A RESULT, TOLLS REVENUE REACHED A RECORD \$419.2 MILLION, UP 4.6 PERCENT FROM THE AMOUNT COLLECTED IN 1993. TOTAL OPERATING REVENUES FOR THE YEAR WERE \$548 MILLION.

OPERATING EXPENSES IN FISCAL YEAR 1994 WERE \$546 MILLION, AN INCREASE OF \$22 MILLION OR 4.3 PERCENT OVER FISCAL YEAR 1993. TONNAGE PAYMENTS TO THE GOVERNMENT OF PANAMA ROSE FROM \$67 MILLION IN 1993 TO \$70 MILLION IN 1994 AS A RESULT OF THE INCREASED TRAFFIC VOLUME. PAYROLL COSTS AT \$298 MILLION WERE UP 4.2 PERCENT, REFLECTING THE 2 PERCENT WAGE INCREASE FOR ALL EMPLOYEES EFFECTIVE JANUARY, 1994 AND A MODEST ADDITION TO OUR MANPOWER RESOURCES REQUIRED FOR THE HANDLING OF ADDITIONAL TRAFFIC VOLUMES. FULL-TIME EQUIVALENTS (FTEs) ROSE FROM 8,459 IN FY 1993 TO 8,535 IN FY 1994.

AT THE BOTTOM LINE, THE COMMISSION HAD NET REVENUES OF \$1.7 MILLION, WITH \$600,000 APPLIED TO RECOVER THE BALANCE OF THE LOSS CARRIED OVER FROM FY 1992 AND THE EXCESS OF \$1.1 MILLION HAS BEEN PAID TO THE GOVERNMENT OF PANAMA IN ACCORDANCE WITH THE REQUIREMENTS OF THE PANAMA CANAL TREATY.

OUTLOOK FOR FISCAL YEAR 1995

FURTHER GROWTH IN TRAFFIC AND TOLLS REVENUE IS ANTICIPATED IN FY 1995 AS THE U.S. ECONOMY CONTINUES TO GROW AND TRADE RECOVERY OCCURS WORLDWIDE. WESTERN EUROPE IS SHOWING A FAIRLY VIGOROUS RECOVERY THAT IS HAVING BENEFICIAL EFFECTS ON SEABORNE TRADE, AND SIGNS OF JAPANESE REVIVAL ARE ALSO EVIDENT. THE FAR EASTERN INDUSTRIALIZING NATIONS' ECONOMIES WILL CONTINUE TO DO WELL IN THE NEAR FUTURE, LED BY FURTHER INCREASES IN THEIR INTERNATIONAL TRADE. ADDITIONALLY, LATIN AMERICAN TRADE WITH THE U.S. AND EUROPE IS EXPECTED TO CONTINUE EXPANDING AS ECONOMIC REFORM IN THE NATIONS OF THIS REGION STIMULATES TRADE AND INVESTMENT.

CANAL TRAFFIC PATTERNS FOR THE FIRST QUARTER OF FISCAL YEAR 1995 SUPPORT THE EXPECTATION OF ADDITIONAL GROWTH THIS FISCAL YEAR. OCEANGOING TRANSITS REGISTERED THE STRONGEST FIRST QUARTER SINCE 1982, TOTALING 3,226 OR 35.1 PER DAY AND TOLLS REVENUE AT \$111 MILLION WAS \$5 MILLION OVER THE \$106

MILLION RECORDED LAST YEAR. COMMERCIAL CARGO TONNAGE FOR THE FIRST QUARTER REACHED THE HIGHEST LEVEL SINCE 1982, INCREASING 7.1 PERCENT TO 45 MILLION LONG TONS WHEN COMPARED TO THE SAME PERIOD LAST YEAR.

COMMODITIES PARTICULARLY SENSITIVE TO THE LEVEL OF ECONOMIC ACTIVITY, SUCH AS MANUFACTURES OF IRON AND STEEL AND COAL AND COKE, SHOWED STRONG GAINS. CONTAINERIZED CARGO SHIPMENTS WERE ALSO UP SLIGHTLY, DUE TO INCREASED TRADE BETWEEN SOUTH AMERICAN COUNTRIES AND THE U.S. EAST COAST AND EUROPE. FURTHERMORE, REFRIGERATED PRODUCTS, GRAINS, AUTOMOBILES, PHOSPHATES AND LUMBER SHIPMENTS FOR THE FIRST THREE MONTHS OF THE YEAR PERFORMED WELL ABOVE LEVELS DURING THE SAME PERIOD OF LAST YEAR.

FOR THE FULL FISCAL YEAR 1995, OCEANGOING TRANSITS ARE FORECAST AT 12,675 OR 34.7 DAILY. TOLLS REVENUE, AT CURRENT TOLL RATES, IS ESTIMATED AT \$428 MILLION, AN INCREASE OF 2.1 PERCENT FROM THE HIGH FY 1994 LEVELS. TOTAL OPERATING REVENUES ARE FORECAST AT \$561 MILLION AFTER DEDUCTING \$12

MILLION FOR THE FINANCING OF OUR CAPITAL EXPENDITURE PROGRAM AND \$5 MILLION FOR WORKING CAPITAL.

OPERATING EXPENSES ARE BUDGETED AT \$561 MILLION OR AN INCREASE OF 2.7 PERCENT OVER THE PRIOR YEAR AND A BREAK-EVEN OPERATION IS FORECAST FOR ALL OF FISCAL YEAR 1995.

BUDGET FOR FISCAL YEAR 1996

TURNING TO THE YEAR UNDER REVIEW TODAY, THE COMMISSION HAS BUDGETED A BREAK-EVEN OPERATION FOR FISCAL YEAR 1996.

TOTAL OPERATING REVENUES (AFTER PROVIDING \$12 MILLION FOR OUR CAPITAL EXPENDITURE PROGRAM AND \$5 MILLION FOR WORKING CAPITAL) ARE ESTIMATED AT \$571 MILLION. TOLLS REVENUE, AT EXISTING RATES (THE LAST CHANGE IN TOLL RATES WAS OCTOBER 1, 1992), ARE FORECAST AT \$435 MILLION.

CANAL TRAFFIC AND TOLLS REVENUE SHOULD CONTINUE A GROWTH PATTERN IN FISCAL YEAR 1996 AS THE U.S. ECONOMY EXPANDS

DURING THE FIRST HALF OF THAT FISCAL YEAR; THE EUROPEAN AND JAPANESE ECONOMIC RECOVERIES STRENGTHEN; AND GROWTH IN THE FAR EASTERN AND LATIN AMERICAN INDUSTRIALIZING NATIONS EXCEEDS THAT IN INDUSTRIALIZED COUNTRIES.

BULK-TYPE COMMODITIES SUCH AS GRAIN, PHOSPHATES, LUMBER AND PRODUCTS; CONTAINER TRADE TO AND FROM WEST COAST SOUTH AMERICA; REEFER TRADE TO EUROPE AND THE U.S. EAST COAST; AND MANUFACTURES OF IRON AND STEEL ARE ANTICIPATED TO CONTINUE DRIVING CANAL TRAFFIC DURING FISCAL YEAR 1996. THE BANANA TRADE IS EXPECTED TO SHOW SOME SMALL GROWTH DUE TO A PLANNED INCREASE IN LATIN AMERICA'S QUOTA BY THE EUROPEAN UNION DURING FISCAL YEAR 1995, WHILE AUTOMOBILE SHIPMENTS SHOULD REMAIN ESSENTIALLY UNCHANGED.

REFLECTING THESE ECONOMIC AND TRADE DEVELOPMENTS, OUR CURRENT ESTIMATES FOR FISCAL YEAR 1996 SHOW OCEANGOING TRANSITS AT 12,850 OR 35.1 DAILY AND TOLLS REVENUE AT \$435.0 MILLION, A 1.6 PERCENT GROWTH RATE.

TOTAL OPERATING COSTS IN FY 1996 ARE ESTIMATED AT \$571 MILLION, AN INCREASE OF 1.8 PERCENT OVER FY 1995. PAYROLL AND RELATED COSTS ARE BUDGETED AT \$321 MILLION AND INCLUDE AN ASSUMED 2.0 PERCENT PAY INCREASE FOR ALL EMPLOYEES EFFECTIVE JANUARY 1, 1996. TREATY MANDATED PAYMENTS TO PANAMA ARE ESTIMATED AT \$95.2 MILLION, AN INCREASE OF 1.3 PERCENT, AS A RESULT OF THE HIGHER CANAL TRAFFIC LEVELS.

IN SUMMARY, THE COMMISSION HAS BUDGETED A BREAK-EVEN OPERATION FOR FY 1996, TO RECOVER ALL COSTS OF OPERATIONS AND THE FUNDS REQUIRED TO FINANCE ITS CAPITAL IMPROVEMENT PROGRAM AND WORKING CAPITAL REQUIREMENTS.

ONE FINAL NOTE ON OUR TRAFFIC FORECAST. A QUESTION THAT HAS BEEN ASKED FREQUENTLY OF US IS WHETHER THE NAFTA OR GATT/WTO AGREEMENTS HAVE SIGNIFICANTLY MODIFIED THE OUTLOOK FOR CANAL TRADE. WE DO NOT EXPECT ANY IMMEDIATE DIRECT IMPACT ON CANAL TRADE FLOWS AS A RESULT OF EITHER ACCORD. OVER THE LONG TERM HOWEVER, IF FREE TRADE AGREEMENTS ARE EXTENDED THROUGHOUT LATIN AMERICA OR IF

GATT/WTO IS SUCCESSFULLY IMPLEMENTED IN COUNTRIES AND REGIONS IMPORTANT TO THE CANAL, THEY COULD SERVE TO POSITIVELY STIMULATE TRADE AND USE OF THE CANAL.

CAPITAL REQUIREMENTS

I WILL TURN NOW TO THE CAPITAL PROGRAM FOR FISCAL YEAR 1996. AS IN PAST YEARS, OVER 70 PERCENT OF THE PROGRAM IS DEVOTED TO ESSENTIAL TRANSIT FACILITIES AND EQUIPMENT. THE MAJORITY OF THESE FUNDS ARE EXPENDED TO IMPROVE TRANSIT SAFETY AND EFFICIENCY, AND TO MODERNIZE THE CANAL. INCLUDED IN THE FY 1996 PROGRAM IS THE REPLACEMENT OF THE TUGBOAT SCHLEY, THE REPLACEMENT OF LAUNCHES, THE UPGRADING OF ALL LOCKS TRANSFORMER ROOMS SWITCHING GEAR, AND THE REPLACEMENT OF OVER-AGE VEHICLES IN THE COMMISSION'S MOTOR TRANSPORTATION FLEET WHICH EXCEED GSA AGE OR MILEAGE STANDARDS.

THE MAJOR CONTINUING PROJECT IN OUR CAPITAL PROGRAM IS THE WIDENING AND STRAIGHTENING OF THE GAILLARD CUT. WE HAVE

BUDGETED \$10 MILLION FOR THIS PROGRAM IN FY 1996, BRINGING THE TOTAL FOR THE YEARS FY 1991 TO FY 1996 TO NEARLY \$41 MILLION.

DRY EXCAVATION WORK IN THE CUT, WHICH IS BEING PERFORMED PRIMARILY BY PANAMANIAN CONTRACTORS, HAS CONTINUED AT A RAPID PACE SINCE FY 1993. SEVEN OF THE TEN CONTRACTS AWARDED HAVE BEEN COMPLETED. ADDITIONALLY, BECAUSE THE BIDS FOR THE DRY EXCAVATION CONTRACT WORK AWARDED TO DATE HAVE CONTINUED TO BE BELOW THE INITIAL ENGINEERING ESTIMATES, WE HAVE BEEN ABLE TO ADVANCE THE WORK AHEAD OF OUR ORIGINAL SCHEDULE FOR THIS PROGRAM.

THE WET EXCAVATION WORK BEGAN IN FY 1994, AS SCHEDULED, AND IS BEING ACCOMPLISHED BY EXISTING "IN-HOUSE" FORCES. THE FIRST PHASE OF THE MARINE-BASED DRILLING AND BLASTING WORK, PROGRAMMED FOR FISCAL YEAR 1994, WAS COMPLETED IN AUGUST AND THE REMOVAL OF THE BELOW-WATER LAND MASS FROM THIS WORK WAS COMPLETED LAST SEPTEMBER.

OF THE \$10 MILLION FOR CUT WIDENING WORK IN FY 1996, APPROXIMATELY \$8 MILLION IS INCLUDED FOR CONTINUATION OF THE DRY EXCAVATIONS, PRIMARILY THE REMOVAL OF 2.7 MILLION CUBIC METERS TO COMPLETE THE THIRD AND FINAL PHASE OF THE CASCADAS PROJECT ON THE WEST BANK. THE BALANCE OF \$2 MILLION WILL FUND DRILLING, BLASTING, AND DREDGING OPERATIONS PLANNED IN THE NORTH SECTOR OF GAILLARD CUT.

FLOATING CRANE TITAN

ANOTHER ITEM OF SIGNIFICANCE RELATED TO OUR CAPITAL EXPENDITURE PROGRAM IS A STUDY WE HAVE COMPLETED ON THE REPLACEMENT OF THE CANAL'S 80-YEAR OLD HEAVY-LIFT CRANE HERCULES WITH THE TITAN, A LARGER HIGH-QUALITY CRANE BUILT IN 1941. THE TITAN WAS RECENTLY EXCESSED AT THE LONG BEACH NAVAL STATION (LBNS), AND MADE AVAILABLE FOR TRANSFER TO THE PCC ON A NON-REIMBURSABLE BASIS.

IN EVALUATING THE TITAN, WE RECEIVED TECHNICAL ASSISTANCE FROM THE U.S. ARMY CORPS OF ENGINEERS MARINE DESIGN CENTER

(MDC) TO REVIEW OUR HEAVY-LIFT ASSIGNMENTS, INSPECT THE CRANE AND EXAMINE THE SCOPE OF WORK TO READY THE CRAFT FOR THE WATERWAY. MDC HAS CONCLUDED THAT THE TITAN CAN OUTPERFORM THE HERCULES AND HAS THE CAPABILITY TO FULFILL ALL OF OUR PRESENT AND FUTURE HEAVY-LIFT NEEDS. ALTHOUGH THE TITAN HAS BEEN KEPT OPERATIONAL, CERTAIN MODIFICATIONS AND RECONDITIONING WOULD BE NECESSARY AT A TOTAL COST OF ABOUT \$12 MILLION.

AS PART OF THE STUDY, WE CONSIDERED OTHER OPTIONS AS WELL, INCLUDING ACQUISITION OF A USED FLOATING CRANE SIMILAR TO THE HERCULES AND CONSTRUCTION OF A NEW, IN-KIND REPLACEMENT. WE HAVE CONCLUDED A WORLDWIDE MARKET SURVEY ON THE AVAILABILITY OF OTHER HEAVY-LIFT FLOATING CRANES, AND DETERMINED THIS ALTERNATIVE CURRENTLY IS NOT FEASIBLE. REGARDING CONSTRUCTION OF A NEW CRANE, MDC ESTIMATES THAT THE COST OF BUILDING A NEW HERCULES COULD REACH \$25 MILLION, THE HIGHEST INITIAL INVESTMENT AMONG OUR OPTIONS.

WE HAVE CONCLUDED THAT REPLACEMENT OF THE HERCULES WITH THE TITAN OFFERS THE GREATEST ADVANTAGES TO THE PCC AND THE BOARD OF DIRECTORS HAS APPROVED THIS ACQUISITION. THE MODIFICATION AND RECONDITIONING WORK TO BE DONE BEFORE MOVING THE CRANE TO PANAMA, IS SCHEDULED TO BEGIN IN JUNE AT THE LONG BEACH NAVAL SHIPYARD.

TRANSITION ACTIVITIES

AT LAST YEAR'S HEARING, I REPORTED ON A NUMBER OF IMPORTANT INITIATIVES UNDERWAY IN PANAMA DEALING WITH THE PLANNING AND PREPARATION FOR THE TRANSFER OF THE CANAL ON DECEMBER 31, 1999. THESE INITIATIVES INCLUDED A CONSTITUTIONAL AMENDMENT CREATING AN AUTONOMOUS PANAMANIAN CANAL AUTHORITY TO OPERATE THE CANAL AFTER THE YEAR 2000. I WOULD LIKE TO BRIEFLY COMMENT ON THIS TRANSITION ACTIVITY AND THE NEW PANAMA TRANSITION COMMISSION APPOINTED BY PRESIDENT PEREZ BALLADARES ON JANUARY 24, 1995.

SHORTLY AFTER HIS INAUGURATION ON SEPTEMBER 1, 1994, I MET WITH PRESIDENT PEREZ BALLADARES, SELECT MEMBERS OF HIS CABINET AND KEY ADVISORS DURING WHICH TOPICS REGARDING THE CANAL AND ITS FUTURE TRANSFER TO PANAMA WERE DISCUSSED. IN THAT MEETING, THE PRESIDENT ASSURED ME THAT HE VIEWS THE PREPARATION REQUIRED TO ENSURE THE FUTURE EFFICIENT AND DEPENDABLE OPERATION OF THE CANAL IS ONE OF THE MOST IMPORTANT CHALLENGES FACING HIS ADMINISTRATION IN THE NEXT FIVE YEARS.

CONSTITUTIONAL AMENDMENT

I AM PLEASED TO REPORT THAT THE NEW PEREZ BALLADARES GOVERNMENT MOVED QUICKLY TO GAIN THE REQUIRED SECOND LEGISLATIVE APPROVAL OF THE CONSTITUTIONAL AMENDMENT PROVIDING FOR THE LEGAL FRAMEWORK FOR AN AUTONOMOUS ENTITY TO ADMINISTER AND OPERATE THE CANAL IN THE YEAR 2000 AND BEYOND. GOVERNMENT EFFORTS ARE ALSO UNDERWAY, VIA THE NEWLY APPOINTED TRANSITION COMMISSION TO DRAFT AN "ORGANIC LAW" IMPLEMENTING THE CONSTITUTIONAL

AMENDMENT. THIS TASK WILL INCLUDE DEVELOPMENT OF THE LEGISLATION NECESSARY TO REGULATE THE NEW PANAMA CANAL AUTHORITY. GIVEN THE IMPORTANCE OF SUCH LEGISLATION TO FUTURE CANAL OPERATIONS, I FULLY EXPECT THAT I AND OTHER COMMISSION OFFICIALS WILL BE ASKED TO PARTICIPATE -- AS ADVISORS OR RESOURCE PERSONNEL -- IN PANAMA'S EFFORTS TO DEVELOP A COMPREHENSIVE PACKAGE OF LAWS TO ADMINISTER POST-1999 CANAL OPERATIONS.

TRANSITION COMMISSION

AS I MENTIONED EARLIER, PRESIDENT PEREZ BALLADARES INAUGURATED A PANAMA TRANSITION COMMISSION ON JANUARY 24, 1995 TO COORDINATE AND OVERSEE FOR PANAMA ALL MATTERS RELATING TO THE TRANSFER OF THE CANAL ENTERPRISE. THIS NEW TRANSITION COMMISSION, WHICH ESSENTIALLY REPLACES A PRESIDENTIAL COMMISSION OF CIVILIAN ADVISORS ESTABLISHED DURING THE ENDARA ADMINISTRATION, RESPONDS DIRECTLY TO PANAMA'S MINISTER OF FOREIGN AFFAIRS. THE COMMISSION INCLUDES THE FOUR NEW PANAMANIAN MEMBER DESIGNATES TO

THE PANAMA CANAL COMMISSION BOARD OF DIRECTORS, THREE PANAMANIAN MEMBERS OF THE TREATY-BASED CONSULTATIVE COMMITTEE, PLUS THE DIRECTOR GENERAL OF CANAL AFFAIRS AND THE EXECUTIVE DIRECTOR OF PANAMANIAN TREATY AFFAIRS EXECUTIVE BUREAU (DEPAT). I PLAN TO PLAY AN ACTIVE ADVISORY ROLE IN THE COMMISSION'S ACTIVITIES AND, IN FACT, WE HAVE ALREADY STARTED THIS RELATIONSHIP.

ON THE PANAMA CANAL COMMISSION FRONT, WE ANTICIPATE THE NEED FOR GREATER AND MORE IN DEPTH COORDINATION WITH THE GOVERNMENT OF PANAMA, THE U.S. DEPARTMENTS OF STATE AND DEFENSE AND OTHERS ON TRANSITION-RELATED MATTERS. IN THAT REGARD, OUR OFFICE OF EXECUTIVE ADMINISTRATION HAS BEEN DESIGNATED AS A CENTRAL POINT FOR TRANSITION COORDINATION.

CONCLUSION

IN CLOSING, I WOULD LIKE TO SUMMARIZE CERTAIN ACTIONS AND ACTIVITIES CURRENTLY UNDERWAY TO PREPARE FOR THE YEAR 2000. WE ARE INVESTING APPROXIMATELY \$125 MILLION

ANNUALLY IN MAINTAINING, MODERNIZING AND IMPROVING CANAL FACILITIES. WE ARE STRIVING TO MAINTAIN A HIGH DEGREE OF PROFESSIONALISM AND MORALE AMONG OUR EMPLOYEES.

TRAINING PROGRAMS TO ENSURE A QUALITY WORK FORCE AND PROVIDE FOR INCREASED PARTICIPATION BY PANAMANIAN THROUGHOUT THE ORGANIZATION REMAIN ONE OF OUR TOP PRIORITIES. PANAMANIAN CITIZENS NOW COMPRISE OVER 89 PERCENT OF THE COMMISSION'S WORK FORCE, WITH INCREASING INVOLVEMENT AT ALL MANAGEMENT LEVELS. PANAMANIAN PILOTS PRESENTLY TOTAL 139 OR 54.9 PERCENT OF THE TOTAL PILOT FORCE.

IN KEEPING WITH OUR OBJECTIVE TO PROVIDE MAXIMUM ASSISTANCE IN THE GOVERNMENT TO GOVERNMENT TRANSITION ISSUES, I CONTINUE TO BE ACTIVELY INVOLVED, ALONG WITH SENIOR MEMBERS OF MY STAFF, IN PRESENTING SPECIALLY DESIGNED BRIEFINGS ON CANAL OPERATIONS. THE PRIMARY THRUST OF THESE PRESENTATIONS HAS BEEN TO IDENTIFY THE POLICIES, SYSTEMS AND FUNCTIONS THAT ARE CURRENTLY

NECESSARY FOR THE SUCCESSFUL MANAGEMENT AND ADMINISTRATION OF THE PANAMA CANAL. DURING THE PAST YEAR, MEMBERS OF MY STAFF AND I HAVE ADDRESSED A VARIETY OF PANAMANIAN GOVERNMENT TASK FORCES, COMMERCIAL FORUMS, SUCH AS MARITIME CONFERENCES AND TRADE CONVENTIONS AND LOCAL ORGANIZATIONS SUCH AS THE PANAMA ASSOCIATION OF BUSINESS EXECUTIVES AND THE PANAMA CHAMBER OF COMMERCE.

AND LASTLY, MR. CHAIRMAN, I WISH TO UNDERSCORE THE COMMENTS MADE BY THE CHAIRMAN REGARDING THE PROPOSED LEGISLATION TO, AMONG OTHER THINGS, CONVERT THE PANAMA CANAL COMMISSION TO A WHOLLY OWNED GOVERNMENT CORPORATION. IT IS IMPORTANT TO THE FUTURE OF THE CANAL AND TO THE UNITED STATES AND PANAMA THAT WE BEGIN THE CONVERSION AS SOON AS POSSIBLE AND I ASK YOUR SUPPORT IN THIS ENDEAVOR.

MR. CHAIRMAN, THAT CONCLUDES MY PREPARED REMARKS. I WOULD BE PLEASED TO ANSWER ANY QUESTIONS THAT YOU OR THE MEMBERS OF THE PANEL MAY HAVE AT THIS TIME.

Mr. BATEMAN. Thank you, Mr. Guardia.

You mentioned that a part of your capital improvement budget was for the acquisition of the heavy lift crane Titan to replace the Hercules.

As I recall on reading your written statement, the Titan is a vintage 1941 crane? I see Mr. Rhode nodding his head.

Mr. RHODE. It is.

Mr. BATEMAN. It comes from Long Beach, CA. Is this the crane that they acquired through some process of reparation at the end of World War II that was a German crane? It is that one, same crane that I saw there several years ago. You look upon it as being a significant upgrade in your capability?

Mr. GUARDIA. The crane has been kept in operating condition. We will be however doing sort of two phases of the \$12 million figure that I mentioned in my statement. One of it is doing some overhaul work for it, to put it in very good, optimum condition.

The other phase is doing work that needs to be done in order for it to navigate from Long Beach to Panama. We have some expenses also in making the whole structure of the crane tropicalized as you may call it.

Those moneys won't be expended in this fiscal year. Actually, they will be expensed in a series, well, at least in a couple of fiscal years.

The crane provides the Commission with a larger capacity to deal with heavy loads. It has more capacity than Hercules which is almost on the borderline of its limits.

We feel even a little unsafe when it goes to its top capacity. The Titan will provide us, again, with a margin in there, plus the fact that the canal, year after year, is handling more and more heavy loads because of the fact that larger ships transit in the canal today, percentagewise, than did many years ago.

Mr. BATEMAN. If you would, very briefly, give me some idea of the types of heavy lift that this crane would be called upon to perform.

Mr. GUARDIA. We may have to lift, for instance, a whole locomotive from the walls of the canal that guide the ships. We may want to lift, for instance, a tug and this crane has the capacity to lift a tug.

Sometimes we need to respond to needs that come about because of transits, really, of ships that may run into difficulty. The crane may help us respond to that. Also, of course, the Midar gates are the very heavy loads that we have to deal with every year.

Mr. BATEMAN. This is a floating crane, I take it.

Mr. GUARDIA. It is a floating crane. The barge has dimensions to maneuver through the locks which is a limitation that is very sensitive in canal operations.

Mr. BATEMAN. Is the crane onsite yet in Panama?

Mr. GUARDIA. No; it is in Long Beach.

Mr. BATEMAN. If you would, I would like a better understanding than I presently have of where the constitutional amendment process stands. Has the constitutional amendment of which you spoke actually been finally adopted and all that remains is the legislative implementation of it?

Mr. GUARDIA. That is correct. The constitutional amendment had to go through two legislative approvals; two independent legislatures. The present administration moved very quickly getting in the agenda of the legislature that is a very high priority. It did get approved. Now, it is part of the Panamanian Constitution, its contents.

Mr. BATEMAN. It does not require any referendum or any further action?

Mr. GUARDIA. No. That system of two independent legislatures' approval does away with that.

Mr. BATEMAN. I now recognize Mr. Taylor for any questions he may have.

Mr. TAYLOR. Thank you, Mr. Chairman.

Mr. Guardia, if you could explain for the people here, there were some concerns that are expressed in our country and privately in your country that the canal at some point would be used as a cash cow for whatever government is in power. That the case that would be taken from the canal would not be available for the continued maintenance that is necessary in order to keep the canal operational and available for the world's traffic.

What sort of assurances are you getting from the Balladares government that, that won't take place? What is the Commission doing from trying to prevent that from happening?

Mr. GUARDIA. Yes; this has been a concern of the users of the canal, on the one hand, that we have been perceiving in our marketing trips to different areas of the world where we have canal users.

It has also been a concern in Panama itself. This is one of the areas to which our briefings on our participation with many groups in Panama have addressed the sensitivity of the canal remaining competitive.

The fact that the canal is not a monopoly, it is not the only option to move cargo in its main route. It could result, if a gorman saw it, as a business in itself rather than seeing the opportunities that a successful canal would have in the country, in many areas of services and other activities that could be related to the shipping industry.

There is one already beginning to develop in Panama which is, a part of it is operative. It is a transshipment port that has developed as one of these types of services that could be developed because of the existence of a waterway that has the level of traffic that the canal has.

The effort to get people in Panama aware in both the private and public sectors of these sensitivities I think that has had a very positive response. I think there is a reason why that constitutional amendment was first put together. It was an indication of the seriousness with which the country was looking at the responsibility of managing the canal.

Then the present administration's subscription of that constitutional amendment which was passed by a different administration from other political parties, I think it is an indication of an awareness being developed in Panama of the importance of keeping a canal that is efficient, that is competitive and that would remain providing a service to the shipping industry.

Mr. TAYLOR. Mr. Guardia, there has been some speculation both, again, in my country and in yours that at some point after 1999, what is then the Panama Canal Commission or the organization that is responsible for the canal, would turn around and sublet the operation of the canal to a private contractor.

What is your opinion of that? Do you see that as a potential? Do you see that as a definite or is it something that probably won't happen?

Mr. GUARDIA. It is something that I almost could say that is something that would probably not happen. I can say that there is definitely not an environment in Panama for that. The Panamanian Government is trying very hard to privatize many activities that are very clear types of activities that are better managed on their private management.

There is always resistance to that. Nevertheless, some privatization has taken place; more slowly than many would hope that it would. In the case of the canal, the canal is too much identified with the country of Panama to be, I think, likely for it to be privatized.

I think there would be a tremendous political resistance to that. Fortunately, I think this has gone in the direction of trying to create an agency that is in effect isolated from partisan politics and that has a level of autonomy and independence.

This is what we are looking at right now from the perspective of what was included in that constitutional amendment and the way that the legislation that is being conformed, even though it is in its beginning stages, but nevertheless it is going to be oriented by that amendment.

Mr. TAYLOR. This is going to be a long question. I hope you can bear with me. The nay-sayers in this country would turn around and look at the rather sizable number of Panamanians involved in the operation of the canal, percentagewise, and say, well, it is not the key people and it is mostly just the day laborers.

For my information and for the information of this committee, What percentage of your pilots are Panamanian, and I'll follow, if you don't mind. The next question would be, Is there a separate engineering team responsible for the actual canal maintenance?

Is there another engineering team responsible for the locks? If you can break it down by groups as to, again, talking at the top of the pyramid, your key people. What percentage of those are Panamanian?

Mr. GUARDIA. I mentioned that now, over 89 percent are Panamanian. Of course, that is a very gross number. The canal operates under three operations bureaus; the Engineering and Construction and Marine Bureaus under General Services.

The Engineering and Construction Bureau deals with all construction and engineering and construction and contracting of the Panama Canal, and all of the power generation activities. At the head of that bureau today is a Panamanian engineer. The deputy is also a Panamanian engineer.

If you go down the line, there are Panamanian professionals in charge of a number of the activities under the responsibility, for instance, of the Engineering and Construction Bureau.

The Dredging Division of the Panama Canal is directed by a Panamanian engineer also. Under the Marine Bureau we have—and the Engineering and Construction is involved in a lot of the maintenance work; especially work that deals with the channel itself, like slide prevention programs and things of that nature. The head of our geotechnical branch is a doctor and geotechnician who is a Panamanian professional.

In the Marine Bureau, the deputy director is a Panamanian professional. The director is Capt. George Hall who is a U.S. citizen. Under that Bureau, for instance, the Locks Maintenance Division is directed by a Panamanian engineer.

I would say that there are professionals in all of the areas, important areas, of the canal. There are also Americans in some of these positions. Normally, there are people either in other bureaus that could move to those positions or even within the same bureau.

We have horizontal mobility in the Panama Canal because of that. You would have situations where, for instance, the present director of a General Services Bureau, who is a Panamanian engineer, that is the third of the three bureaus, came from the power generation branch within the Engineering and Construction Bureau.

He had good management capabilities. So, he was moved from the Engineering and Construction Bureau to the General Services Bureau to head that bureau. That takes place within the Panama Canal organization. I am not too concerned about that.

In the area of pilots, which is perhaps the most difficult area in that respect because Panama is a small country that doesn't generate natural pilots, especially Panama Canal pilots. So, a tremendous effort is being done in that area, to the point that where the treaties were implemented in 1979, there were just four Panamanian pilots in the pilot force. Today, there is over 50 percent Panamanian pilots in the pilot work force.

The progression in that area has had tremendous impact. In that area, of course, because of the fact that it takes years to train a Panama Canal pilot, to the point that we couldn't really import pilots from other waters.

They would still have to go through a training program to get the expertise, to assume responsibility for a ship crossing the waterway and getting into locks with the very tight squeezes that we have in the canal.

In that program, we monitor that continuously to make sure that we have people in the pipeline to achieve a 100-percent Panamanian work force. The last review that we have indicates to us that we will achieve that. We may not have exactly 100 percent. We may have 98 percent, but we are going to be close to it.

Mr. RHODE. Mr. Chairman, if I might supplement the Administrator's comments.

Mr. BATEMAN. Sure.

Mr. RHODE. I think that you can see from what he has set forth that the inclusion of Panamanians into the work force has been very impressive since implementation of the treaty.

At the same, I think Mr. Guardia is probably one of the most outspoken champions of this. Every effort is being made today to

ensure that the prism we look at when we look at the work force is one that is neutral.

There are a number of U.S. citizens who are invaluable employees of the canal. I think that the attitude of the current administration and certainly the board is that these employees will be treated professionally, based on the merits.

We don't anticipate anything transpiring when you go from December 31, 1999, to January 1, the year 2000. That is our goal. We want the commercial world. It is important that the commercial world perceive that there is no dramatic change.

Mr. TAYLOR. If you don't mind, Mr. Chairman, the last couple of questions.

Mr. BATEMAN. In fairness, if you could, make them brief.

Mr. TAYLOR. Mr. Guardia, what, as far as the direct transfer of funds from the canal to the Government of Panama for noncompensated services, would that amount have been last year? I am seeing a couple of different numbers. I am seeing \$1.1 million in one place and then a larger amount in another; actual cash transfers to the Government of Panama.

Mr. GUARDIA. There are the three items of payments to Panama; two fixed amounts of \$10 million; one, which is an annuity and the other one which is a payment for services rendered to the Commission. Plus, a number that is based on 30-something cents per percent ton that crosses the canal. Among those three numbers, the moneys paid last year, 35 cents per ton, yes, is the present tonnage payment.

It was around \$90 million. This is within what we consider costs as far as our operation. When we say that the canal is a break-even operation, it includes those payments to Panama. Last year, we had a surplus over and above those costs, including the payments to Panama of \$1.1 million, which is the additional payment that was paid in accordance with the Panama Canal Treaty.

Actually, the surplus was \$1.7 million; \$600,000 were used to cover carryover losses. The net result of that was the \$1.1 million that was transferred.

Mr. TAYLOR. So, the total transfer then would have been \$96.7 million.

Mr. GUARDIA. No.

Mr. TAYLOR. \$95.2 million plus \$1.1 million.

Mr. GUARDIA. Plus \$1.1 million, yes.

Mr. TAYLOR. Thank you, sir. Thank you, Mr. Chairman.

Mr. BATEMAN. Thank you, Mr. Taylor.

Now, the gentleman from California, Mr. Cunningham, the vice chairman of the panel.

Mr. CUNNINGHAM. Thank you, Mr. Chairman.

I don't have a whole lot. Most of the area has been covered. I think Mr. Guardia that you can see that most of our concerns are about the security which is in the best interest of Panama and the United States, and the other nations as well.

It is not a partisan issue. It is a very bipartisan issue, what our future is going to be with the canal, and the security of that. I laud your ideas of privatization. We are trying to do the same thing with our Government back here.

At the same time, I realize that even things like our own FAA, and I think it has been discussed that there is better private government participation mainly because if something fails, who is going to pickup the pieces, like with the FAA?

I guess my real question is that I spent 20 years of my life in the U.S. Navy. I am always looking at the aspects when we talk about the security, the engineering, the maintenance, the upkeep.

I have also flown over the Panama Canal when we had our boats going through there. When we turn this over, is there going to be adequate security for the canal? I look at our potential threats around the Nation, Iraq, Iran, Libya, potential terrorist threats.

Are there any preparations to increase as we diminish our role in the Panama Canal the security of the canal itself?

Mr. GUARDIA. Yes. Actually, I would say since treaty implementation, even though the Panama Canal Zone police function was transferred to the Republic of Panama, however, the canal began to implement, and has been continuously upgrading and better equipping a canal protection division. This is essentially an industrial type protection. This means that all of the sensitive structures of the Panama Canal are under surveillance, manned surveillance, and monitored by a closed circuit TV system with alarms and emergencies.

Recently, we inaugurated an additional upgrade of that where we can move from centralized point cameras, even change the areas that they are covering in a particular instance. This way, we are aware of everything that is going on in all of the sensitive structures.

Besides that, we patrol. We have joint patrols of the waterway with the Panamanian Canal area police. There is a canal area police branch of the Panamanian Police that conducts joint patrols with our canal security people.

This has been in a mode of constant improvement. I think that we are all aware that terrorist attacks are something that it is impossible to defend against them with armies or with that type of response capability. Normally, these are the things that are done under surprise.

Mr. CUNNINGHAM. What I was alluding to mostly was I would hope that our own overseas intelligence would work with Panama. Quite often, you can't—you know circuit TV is nice. You can watch it blow up if you want.

I think to prevent those kinds of things that the intelligence that is going to be needed to protect the canal with not only the United States, but Great Britain and our allies, I would hope that they would tap into those kinds of information systems that would prevent anything because it is a real threat.

As I opened this statement, we are concerned about the security of the canal and its importance not only to us, but to the rest of the world. I think you would find our support of those endeavors quite strong.

Mr. GUARDIA. There is in place a communication line or bridge of intelligence. Today, perhaps more related to the drug issue than to terrorist type of operations, but inclusive of, in the sense that there is interchange of information between Panamanian entities and United States entities.

They have been very successful in some drug operations and normally are caught because of intelligence interchange more than a casual actual detection in the border or anything like that.

Mr. CUNNINGHAM. Thank you, Mr. Chairman. I have no further questions.

Mr. BATEMAN. Thank you, Mr. Cunningham.

Now, the gentleman from Rhode Island, Mr. Kennedy.

Mr. KENNEDY. Thank you, Mr. Chairman.

I have no questions at this time. Thank you.

Mr. BATEMAN. Let me offer a comment with regard to the legislation that has been drafted for Congress' consideration.

Presently, I can't tell you a timeframe within which we will deal with it, but I assure you we will deal with it. I will be discussing that with the chairman of the full committee, the gentleman from South Carolina, Mr. Spence. We will get back to you as what we foresee as a legislative track for it.

Not having really looked at the specifics of it, I don't want to make any commitment for myself. I certainly can't make any for anyone else. Indeed, we will attend to it. I certainly will not be looking at it with any negative points of view at the outset.

I have one other area that perhaps is more appropriately addressed to other witnesses. In addition to the Panama Canal, the resources, the assets, the facilities that it represents, we have through the years maintained significant military facilities in the Panama Canal Zone.

These, as I understand it, are to be phased out from American ownership and operation between now and 1999. Is this something that the Panama Canal Commission is directly involved in or is this being handled government-to-government or through other vehicles?

Mr. REEDER. Mr. Chairman, we are not at the canal directly involved. As you know, I wear two hats. We are very well coordinated. Our primary concern, and I am repeating, is to ensure that on the first day after the transition it appears not only is, but appears, and I stress that, seamless. From that standpoint, there will be absent any changes in the course we are on now, something different.

That being what you alluded to, the military presence. We are monitoring that. It is not something we are directly involved in. When I say, "we," I am speaking in my capacity as Chairman of the Panama Canal Commission.

There will be a difference if the commercial world—I think the commercial world will perceive that as a change. I think a lot will depend on things that we can't today see. What is the situation in the world? What is the degree of tranquillity or unrest in that particular part or region of the world?

Those kinds of issues will obviously have a lot to do with whether and to what extent that reality is perceived as something threatening. I just have to underscore something that the Administrator said earlier.

It is imperative that the canal remain competitive. The very first question from Congressman Taylor spoke to that; the concerns about cash cow. That obviously would never work if the resources are taken out of the canal and not available to ensure that the

canal can operate competitively. There are most certainly other alternatives to move in transport cargo.

Mr. BATEMAN. Thank you, Mr. Secretary.

The gentleman from Maine, Mr. Longley.

Mr. LONGLEY. I have no questions at this time. Thanks.

Mr. BATEMAN. The gentleman from Florida, Mr. Scarborough.

Mr. SCARBOROUGH. Thank you, Mr. Chairman; no questions at this time.

Mr. BATEMAN. The gentlelady from California, Ms. Harman.

Ms. HARMAN. No thank you, Mr. Chairman, at this time.

Mr. BATEMAN. I believe we are back to the distinguished ranking member, Mr. Taylor.

Mr. TAYLOR. Mr. Guardia, would you for the purposes of informing the committee, tell the committee what the numbers were in the last poll when the people of Panama were asked if the treaties should be negotiated for the purpose of allowing the Americans to retain their military bases? What percentage of Panamanians were in favor of that?

Mr. GUARDIA. That is a little difficult for me because I have to admit that I don't have the latest numbers on that. I can say that there was a majority shown on the polls that have been taken of support for some sort of negotiations to take place in that respect.

This is from the population. You are aware, as everybody is in Panama of course, that the military drawdown will create, as it does in other areas, as it does here in the United States proper, a vacuum on jobs that are very sought after by the Panamanian labor force.

This is creating a level of concern, especially on the work force, on the labor area of Panama, and in other sectors also. I am sorry that I don't have the number of the last poll. That is something that we can get and submit for the record so that you have it on the record. It is a majority, clear majority.

Mr. TAYLOR. Just for my information because I don't know the answer.

[The information referred to follows:]

On March 28, 1995 Panama City's newspaper La Prensa published a public opinion poll conducted on March 17, 18, and 19 by the Ditcher & Neira consulting firm. According to the newspaper this poll "has a maximum margin of error of about 3 percent"—1,212 people age 18 or older in all provinces of Panama were asked: Do you or do you not want the U.S. military bases to remain after the year 2000? The majority of those surveyed, 69.5 percent, want the U.S. military bases to remain on the shores of the Panama Canal with 17.4 percent saying they do not want the bases to stay. In December 1994, 67.7 percent of those polled supported the continued presence of U.S. military bases and 24.2 percent opposed the continued presence of the bases. The current response level represents a 7-percent decline from the previous figures.

Most of those surveyed who agree with the presence of the military bases live in Panama province (75.5 percent), while in the rest of the Republic those who share this opinion comprise 63.3 percent. Most of those who agree with the presence of the bases, are age 50 or older (74.3 percent). More women (71.7 percent) than men (67.2 percent) want the bases to stay.

Mr. TAYLOR. Do any of your contingency plans at present have a point where they call on the American military to get involved, should there be a problem within the confines of the canal?

I point back to my days in local government. There are certain things our St. Louis police force did. When we had a problem with that, we called the county. When we had problem with that, we called the National Guard.

Mr. REEDER. In Panama, I think that would be a different situation because there is a political line in there that would have to be crossed. The way that we are structured is really, when we have any type of problem in the Commission today, we really go to the Panama area police.

We have close coordination with the military. We keep them informed and visa-versa. On security issues of the Panama Canal, unless there is a major world conflict that is close to Panama in any way, challenges the Panama Canal, there would communication of that type.

The normal operation, at least since I have been Administrator, has been a direct coordination between the canal security and the Panama Canal area police. We have very close coordination even with a drawdown.

This is something that I wanted to get in here. Because of the fact that the military bases are, in many cases, in canal operating areas, there is a very high level of coordination between the Panama military and the Panama Canal Commission. We have a group that meets regularly and that keeps informed on both directions of possible impacts that a transfer of property could have on either of the two agencies; the military enterprise or the Commission.

Mr. REEDER. If I might just supplement that. In the immediate aftermath of Just Cause, the military steps in. There are contingency plans if and when circumstances require.

Mr. TAYLOR. No further questions, Mr. Chairman.

Mr. BATEMAN. Just references to the polls suggesting some body of opinion within the Panamanian citizenry of continued American military presence appears to be a large measure of economic phenomenon of concern that the jobs will go away.

I think reference was made to the same concerns that some communities in this country have when you talk about base closures in that community. So, we find that very understandable.

I wonder if it would be in any way a helpful pursuit, not so much for us, but for Panama if we were to subject those facilities to the base closure analysis process that has been worked out by our military departments to determine what the pros and cons of the operating cost of the facilities as opposed to continuing them open.

Mr. REEDER. It is a very intriguing question, Mr. Chairman. I would think that the follow-on panel might have a view.

Mr. BATEMAN. I don't ask you to take a position on that today. If you would, think about it. It is just an idea off the top of my head as we talked about the natural concerns from the closing of basis.

Mr. REEDER. Yes, sir; I think a process like that is underway. It may not be following statutorily the criteria, the eight or nine criteria of the Base Realignment and Closure Act. However, business-

like decisions are being made as the drawdown proceeds with regard to which installations we should remain in. Those decisions would be similar and businesslike as are the BRAC criteria.

Mr. BATEMAN. Wear your Army hat at this point, Mr. Secretary. Could you get us an inventory of all of the facilities and sort of an update as to the current state of thinking as to time of devolution to Panamanian control between now and 1999 as to all of those facilities? We would like to see that if it is doable.

Mr. REEDER. Mr. Chairman, we can certainly do that. I might simply say that the time lines have slipped. That happens. That happens under BRAC as well. They have slipped. We can give you our best regards to time lines.

Mr. BATEMAN. I'm not asking for you to give us anything that you would feel that you are embarrassed if you did not totally adhere to it, but current state of thinking.

[The information requested by Mr. Bateman follows:]

15 OCTOBER 1994 PC TIP SITE TRANSFER SCHEDULE

1995	1996	1997	1998	1999
Cristobal High School	Caruana Flats	Albrook AF Station	Gorgas Hospital	Fort Kobbé
Fort Davis (cable commo site; launch landing and Dock 45 to POC)	Ft Amador Army - Sep 96 Ft Amador Navy - Sep 96		Panama Canal College Quarry Heights Herrick Heights East Cervati (old Training Complex & Commissary) Margay Avenue Ft Amador (J-Suit Bldg)	Cocodi West Cervati (East and West) East Cervati (Tog Complex) Cervati Commissary Cervati Laundry Cerro Gordo Communications Building 1501 - Balboa (MTN/C)
Fort Knapar				Fort Sherman
Margarita School Bldg				Pisa Training Area
Mundi Veterinary Clinic				Olivia Oliver (antenna site)
Gambon Elm School				Balboa Elementary School
Cerro Pelado (to POC)				Balboa High School
Diablo Elem School				Arcos Hill Communications
Los Rios Elem School				Fort Clayton
				Fort Davis (commo site)
				Ammo Supply Point #1
				Empire Range
				Cervati Middle School
				Howard Air Force Base
				Balboa West Range
				Rodman
				Farfan
				Arraijas Tank Farm
				Marine Corps Barracks

As of: 15 August 1985

TREATY IMPLEMENTATION PLAN COMPLETED AND PROJECTED FACILITY TURNS

COMPLETED:

<u>YEAR</u>	<u>FACs</u>	<u>NO. ACRES</u>	<u>DESCRIPTION/LOCATION</u>	<u>CONGR</u> <u>TO NOTIF</u>
1991	119	287.80	Gatun Tank Farm (Navy)	ROP 1991
	25	14.80	Coco Solo Fam. Hsg (Army)	ROP 1991
Total	144	302.60		
1992	6	7.70	Coco Solo Elem. School (Army)	ROP 1991
	22	29.30	Coco Solo Comm. Bldgs (Army)	ROP 1991
		4.50	Slab Bldg. 1081, Albrook (Army)	ROP 1991
		2.10	NBC Chambers, Albrook (Army)	ROP 1987
		0.22	Slab Bldg. 1143, C. Solo (Army)	ROP
Total	28	43.82		
1993	1	0.80	Bldg. 1002, Curundu (Army)	ROP 1992
	27	8.21	BOQs, Curundu (Army)	ROP 1992
		680.00	Camp Chagres (Army)	ROP 1987
	1	3,503.50	Chlva Chlva Trng. Area (Army)	ROP 1992
Total	29	4,190.51		
1994	51	40.55	Coco Solo Clinic (Army)	ROP 1993
	1	0.00	Bldg. 39-C, Balboa (Army)	ROP 1993
	30	395.88	Summit Radio Station (Navy)	PCC
	2	2.85	Bldgs 1214/1224, Amador (Navy)	ROP 1993
	7	8.15	J-Staff Bldgs, Amador (Navy)	ARM 1993
Total	91	447.23		
1995	18	14	Margarita School Complex (Army)	ROP 1993
	40	65	Crist. Jr-Sr High School (Army)	ROP 1991
	7	1.70	Amador (Navy)	ROP 1993
	3	3.23	Farfan Bldgs (Navy)	AF
	28	708.84	Galeta Island (Navy)	ARM
Total	94	780.77		
GTotal	386	5784.83		

As of: 15 August 1995

TREATY IMPLEMENTATION PLAN COMPLETED AND PROJECTED FACILITY TURNOVERS

PROJECTED:

YEAR	FACs	NO. ACRES	DESCRIPTION/LOCATION	TO	CONGR NOTIF.
1995	321	346.00	Fort Gulick/Espinar (Army)	ROP	1993
	28	279.00	Cerro Pelado Ammo. (Army)	PCC	
	544	3,759.40	Fort Davis (Army)	ROP	1993
			Mindl Veterinary Clinic (Army)	ROP	
	62	91.2	Dock 45/Bldg 61 (Army)	PCC	1993
	5	3.10	Gamboa Elem. School (Army)	ROP	
	10	237.00	Summit (Army)	PCC	
	8	6.91	Los Rios Elem. School (Army)	PCC	1992
		300	Empire Rnge (Army)	ROP	
	7	9.09	Diablo Elem. School (Army)	ROP	1992
Total	975	5,029.70			
1996	304	136.02	Curundu Flats/Trl. Sites (Army)	ROP	1993
	1	0.3	Bldg. 821, Curundu (Army)	ROP	1992
		4,100.00	Empire Rnge (Army)	ROP	
	204	151.8	Fort Amador (Army)	ROP	1993
	2	0.30	Bldg. 352, Fort Amador (Army)	ROP	1993
	58	48.41	Fort Amador (Navy)	ROP	1993
Total	567	4435.83			
1997	87	162.90	Albrook AFS (Army)	ROP	
	510	818.00	Albrook AFS (Air Force)	ROP	
Total	597	768.90			
1998	2	10.60	Panama Canal College (Army)	ROP	
	7	8.15	J-Staff Bldgs, Amador (Army)	ROP	
	255	61.02	Morgan Ave/Quarry. Hts (Army)	ROP	1992
			Herrick Hts/Ancon Commo (Army)	ROP	
	119	35.18	Corozal East (Army)	ROP	
			Gorgas Hospital (Army)	ROP	
Total	383	114.85			

As of: 15 August 1985

TREATY IMPLEMENTATION PLAN
COMPLETED AND PROJECTED FACILITY TURNS

PROJECTED:

YEAR	FACs	NO. ACRES	DESCRIPTION/LOCATION	TO	CONGR NOTICE
1989	201	17,228.00	Empire Range (Army)	ROP	
	6	25.67	Balboa HI School & Elem. (Army)	ROP	
	4	30.52	Curundu Jr HI School (Army)	ROP	1983
	1	2.18	Bldg. 420, Curundu (Army)	ROP	1992
	3	4.41	Bldg. 1087, Curundu (Army)	ROP	1993
	3	1.54	Corozal Commissary (Army)	ROP	
	61	33.78	Diablo Terrace, Corozal (Army)	ROP	
	25	706.84	Galeta Island (Army)	ROP	
	379	23,079.00	Ft Sherman/Pina Range (Army)	ROP	
			Commo Site, Ft. Davis (Army)	ROP	
	439	3,378.20	Fort Kobbe (Army)	ROP	
	2		** Ft Kobbe-C. Gordo (Army)	ROP	
	129	80.20	Cocoll (Army)	ROP	
			Ancon Hill Commo (Army)	ROP	
	9	1.88	Curundu Laundry (Army)	ROP	1992
	59	489.47	Chiva Chiva FBIS & TTS (Army)	ROP	
	144	2,111.89	Rodman Ammo Area (Army)	ROP	
			Czal East-Vet & Bank (Army)	ROP	
	1,375	2,179.97	Fort Clayton (Army)	ROP	
			US Army Mortuary	ROP	
	415	267.43	Czal Industrial-West (Army)	ROP	
	1	0.50	Bldg. 1501, Balboa MTMC (Army)	ROP	
	728	4,475.40	Howard AFB (Air Force)	ROP	
	3	147.00	Horoko Club (Air Force)	ROP	
	0	8,815.40	Balboa West Range (Air Force)	ROP	
	3	40.00	Semaphor Hill (Air Force)	ROP	
	128	600.00	Rodman Naval Station (Navy)	ROP	
	11	77.80	Rousseau Area, Cocoll (Navy)	ROP	
	76	819.70	Farfan Radio Station (Navy)	ROP	
	9	807.20	Arraljan Tank Farm (Navy)	ROP	
	29	133.70	Marine Barracks Annex (Navy)	ROP	
Total	4,242	85,547.27			
GTotal	8,764	75,896.55			

FACs: Any physical structure with a real property record regardless of size

Mr. REEDER. Yes, sir.

Mr. BATEMAN. Mr. Cunningham has another question.

Mr. CUNNINGHAM. Thank you.

I just thought of something. This is for my own information. Once the canal turns over to Panama, is there anything in the treaty that says if the United States had another Desert Storm in a different part of the world, but something like that where we had to get our RO/RO's through we had to get specific types of ships to support combat operations, is there anything in the treaty that gives the United States priority in those kinds of situations?

Mr. REEDER. There is. I don't know if it is an addendum. Mr. Rhode might know the specifics of that. There is a neutrality clause. Is that part and parcel of the treaty?

Mr. RHODE. I believe so. We can provide that for the record, Mr. Cunningham. I think we will need to do a little research on that.

Mr. CUNNINGHAM. Thank you. We would rather work that way than taking it back.

Mr. REEDER. I would like to be very specific with that.

Mr. CUNNINGHAM. That would be nice for the record.

Mr. REEDER. Thank you.

[The information referred to follows:]



OFFICE OF
THE SECRETARY

PANAMA CANAL COMMISSION

INTERNATIONAL SQUARE
1825 I STREET, NW., SUITE 1050
WASHINGTON, DC 20006-5402



April 4, 1995

The Honorable Herbert H. Bateman
Chairman
Special Oversight Panel on the Merchant Marine
2120 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Bateman:

This letter is to supplement the record of the March 28, 1995 hearing before the Panel regarding the Panama Canal Commission. In that hearing, Vice Chairman Cunningham had inquired whether the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal (the Neutrality Treaty) specifically allows for the expedited passage of U.S. military vessels, when necessary.

The witnesses appearing on behalf of the Commission had asked to defer giving an authoritative answer until the relevant materials could be consulted, to ensure the accuracy of our response. We are pleased to provide that here to Vice Chairman Cunningham and to the Panel.

The short answer to Vice Chairman Cunningham's question is that U.S. war and auxiliary vessels are, and will be, entitled to priority in their use of the Panama Canal. Because the Neutrality Treaty is permanently in force, this priority is, and will be, available both before and after the expiration of the associated Panama Canal Treaty on December 31, 1999.

Article II of the Neutrality Treaty generally declares that the Canal, both in time of peace and war, shall remain secure and open to peaceful transit by the vessels of all nations on a non-discriminatory basis. More specifically, however, Article VI provides that, notwithstanding any other provision of the Treaty, vessels of war and auxiliary vessels of both the United States of America and the Republic of Panama "will be entitled to transit the Canal expeditiously." Article VI then defines that statement to mean that such vessels be assured of transit "through the Canal as quickly as possible, without any impediment, with expedited treatment, and in case of need or emergency, to go to the head of the line of vessels in order to transit the Canal rapidly."

TELEPHONE: (202) 634-6441

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The Honorable Herbert H. Bateman
April 3, 1995
Page Two

Attached please find a reproduction of the text of Article VI of the Neutrality Treaty. You will note that part of its language was inserted as an amendment insisted upon by the United States Senate and contained in the United States Instrument of Ratification signed June 15, 1978. Of course, please let us know if we can provide the Panel with further information on this, or any other subject.

Sincerely,


Michael Rhode, Jr.
Secretary

Enclosure

cc: The Honorable Randy "Duke" Cunningham (w/ enclosure)

TREATY CONCERNING THE PERMANENT NEUTRALITY AND OPERATION OF THE PANAMA CANAL

The United States of America and the Republic of Panama have agreed upon the following:

* * * *

ARTICLE VI

1. In recognition of the important contributions of the United States of America and of the Republic of Panama to the construction, operation, maintenance, and protection and defense of the Canal, vessels of war and auxiliary vessels of those nations shall, notwithstanding any other provisions of this Treaty, be entitled to transit the Canal irrespective of their internal operation, means of propulsion, origin, destination, armament or cargo carried. Such vessels of war and auxiliary vessels will be entitled to transit the Canal expeditiously.

2. The United States of America, so long as it has responsibility for the operation of the Canal, may continue to provide the Republic of Colombia toll-free transit through the Canal for its troops, vessels and materials of war. Thereafter, the Republic of Panama may provide the Republic of Colombia and the Republic of Costa Rica with the right of toll-free transit.

* * * *

DONE at Washington, this 7th day of September, 1977, in the English and Spanish languages, both texts being equally authentic.

U.S. Instrument--Neutrality Treaty

JIMMY CARTER

President of the United States of
America

TO ALL TO WHOM THESE PRESENTS
SHALL COME, GREETING:

CONSIDERING THAT:

The Treaty Concerning the
Permanent Neutrality and Opera-
tion of the Panama Canal (Neutra-
lity Treaty) was signed at
Washington on September 7, 1977;
and

The Senate of the United
States of America by its resolu-
tion of March 16, 1978, two-
thirds of the Senators present
concurring therein, gave its
advice and consent to ratifica-
tion of the Neutrality Treaty,
subject to the following:

(a) AMENDMENTS:

* * * *

(2) At the end of the first
paragraph of Article VI, insert
the following:

"In accordance with the
Statement of Understanding men-
tioned in Article IV above: 'The
Neutrality Treaty provides that
the vessels of war and auxiliary
vessels of the United States and
Panama will be entitled to
transit the Canal expeditiously.
This is intended, and it shall so
be interpreted, to assure the
transit of such vessels through
the Canal as quickly as possible,
without any impediment, with
expedited treatment, and in case
of need or emergency, to go to
the head of the line of vessels
in order to transit the Canal
rapidly.'"

* * * *

NOW, THEREFORE, I, Jimmy Carter, President of the United States of America, ratify and confirm the Neutrality Treaty, subject to the aforementioned amendments, conditions, reservations and understandings, and on behalf of the United States of America undertake to fulfill it faithfully.

IN TESTIMONY WHEREOF, I have signed this instrument of ratification and caused the Seal of the United States of America to be affixed.

DONE at the city of Washington this 15th day of June in the year of our Lord one Thousand nine Hundred seventy-eight and of the independence of the United States of America the two hundred second.

By the President:
JIMMY CARTER

Acting Secretary of State
WARREN CHRISTOPHER

Mr. BATEMAN. Does any other member have further questions? If not, we thank you very much for your testimony. I am sure we will be in ongoing communication as we work through the issues with your legislation and your authorization bill.

Thank you very much for being here.

Our next panel consists of Ms. Anne Patterson, the Deputy Assistant Secretary for Central America of the State Department who is accompanied by Brig. Gen. John R. Walsh, the Assistant Deputy for Political Military Affairs of the Joint Staff.

Thank you very much for coming. We look forward to your testimony. Your written statements will be made a part of the record. You can proceed with your own testimony as you may choose, starting with Ms. Patterson.

STATEMENT OF ANNE PATTERSON, DEPUTY ASSISTANT SECRETARY FOR CENTRAL AMERICA, DEPARTMENT OF STATE

Ms. PATTERSON. Mr. Chairman, I am pleased to appear before you and members of the panel today to convey to you the administration's thinking on Panama. Because of its location, Panama has long merited special consideration from the United States.

I have provided more detail in a written statement which has been made available to the panel. Mr. Chairman, this panel has special interest in the possibility of a United States military presence after December 31, 1999, when according to the Panama Canal Treaty, the canal will be under Panamanian ownership and control.

There will no longer be U.S. military bases in that country. Let me say, Mr. Chairman, that the question of remaining in Panama is now under review in the United States Government. This is a complex issue, involving an evaluation of our security interests and an analysis of the cost of various options.

We look forward to working with the Congress as this process unfolds. As 1999 approaches, there are three specific and related areas which are covered by treaty provisions and which are crucial to our relationship with Panama.

The first is the transfer of the Panama Canal. The second is the reversion of the military bases. The third issue is canal security in the post-2000 period. The treaty provides that Panama shall assume responsibility for management, operation, and maintenance of the canal as of December 31, 1999.

The efficient and secure operation of the canal is our primary strategic interest in Panama. Although the development of containerized shipping has reduced the canal's importance for U.S. commerce, it remains important for global commerce and for use by our Armed Forces in wartime.

The Government of Panama will be able to run the canal after 1999. In fact, the Panamanians are largely running it now. It is important to understand, however, that the treaty transfers only the canal's physical assets to Panama. It will not transfer the management structures.

In the next several years, we must establish a management arrangement which will provide for the retention of skilled high-level employees of all nationalities into the post-2000 period.

The U.S. Government has recently proposed legislation to convert the Panama Canal Commission into a government corporation.

The proposed changes are intended to anticipate the semi-autonomous corporate type successor organization which is contemplated by a constitutional amendment just passed by the Panamanian Government.

The Panamanians are now moving forward toward introducing implementing legislation for their canal organization. A conference of canal users is also planned for 1997 to demonstrate preparations that the Panamanians have made to manage the canal.

The second issue of concern to us is the reversion of the military bases. Between now and the end of 1999, the United States plans to return some 77,000 acres with almost 4,300 buildings. The record of Panamanian usage of facilities turned back so far has been mixed.

We will be working closely with the Panamanians to plan and coordinate property returns. This process of consultations should result in a smooth flow of returning facilities in good condition. The sooner we can give the Panamanians a definitive answer about our intentions, the better they can plan their own use of the reverted properties.

The third issue is the consideration of a post-2000 military presence. Our policy is to comply fully with the canal treaties, including the complete withdrawal from Panama by December 31, 1999. As I said, we are reviewing the possibility of a post-2000 presence.

We are working closely with the Defense Department to address the issues involved, including the undeniable utility of the base to fight drug trafficking and for training U.S. forces. As we look at potential benefits, we must also consider the potential costs involved for basing rights.

We will also evaluate whether United States presence will be supported by Panamanians over the long term. Our relationship with the new government of Ernesto Perez Balladares has been very positive. We will be in touch with the Government of Panama to discuss these issues at the appropriate time.

We would welcome consultations with the Congress and especially this panel as we continue this process. Thank you, Mr. Chairman.

Mr. BATEMAN. Thank you, Ms. Patterson.

[The prepared statement of Ms. Patterson follows:]

TESTIMONY BY STATE DEPARTMENT
DEPUTY ASSISTANT SECRETARY FOR INTERAMERICAN AFFAIRS
ANNE PATTERSON
BEFORE THE HOUSE NATIONAL SECURITY COMMITTEE,
SPECIAL OVERSIGHT PANEL ON THE
MERCHANT MARINE

U.S. STRATEGIC INTERESTS IN PANAMA

MARCH 28, 1995

Mr. Chairman, I am pleased to appear before you and members of the Special Oversight Panel today to convey to you the Administration's thinking on Panama. This small, strategically-located isthmus with a population of 2.5 million people has long merited special consideration in United States policy. From the moment of Panamanian independence in 1903, this country has maintained an extraordinarily complex and normally productive relationship with the government and people of Panama.

You will recall that during the 1960's and 70's -- a period of burgeoning nationalism in Panama as well as elsewhere in this hemisphere and the world -- successive Panamanian governments demanded an end to U.S. sovereign-like rights in the Canal Zone and to the concept of perpetual U.S. control over the Canal. President Johnson agreed to negotiate on treaty rights in 1964. The subsequent lengthy negotiations resulted in the Panama Canal Treaty and the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal. These agreements were fully ratified by our two countries in 1979 and have been strictly observed by both parties since then.

The Noriega years, however, were a major exception to the close cooperation on shared aims that has characterized our relationship with Panama throughout the century. General Manuel Noriega assumed dictatorial powers, endangered American lives and property with assaults and declared war on the United States. Operation Just Cause unseated Noriega and allowed the reestablishment of democracy in Panama. President Guillermo Endara and his government concentrated their efforts on grounding democracy more firmly.

The current government of Panamanian President Ernesto Perez Balladares is a result of free and fair elections last year. There are unprecedented levels of support in Panama for democracy. The U.S. government enjoys a particularly smooth relationship with the Government of Panama, which I will be pleased to address later.

TREATY PROVISIONS

Mr. Chairman, some members of Congress have indicated special interest in the subject of a possible United States military presence after December 31, 1999 when, according to the Panama Canal treaties, the Canal will be under Panamanian ownership and control, and there will no longer be United States military bases in that country. As you know, we intend to comply fully with the provisions of those treaties.

As the year 2000 approaches, there are three specific and related areas covered by treaty provisions which are crucial to our relationship with Panama. The first is the transfer of the Panama Canal to the Government of Panama. The second is the reversion of properties currently used for United States military basing to the Panamanian Government. The third area concerns the U.S. security relationship with Panama and the Canal.

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PANAMA CANAL

Let me briefly review first the specific treaty provisions governing the transfer of the Panama Canal to the Panamanian Government. Article XIII (1) of the Panama Canal Treaty provides that upon termination of the treaty at noon on December 31, 1999, the Panamanian government "shall assume total responsibility for the management, operation, and maintenance of the Panama Canal, which shall be turned over in operating condition and free of liens and debts, except as the two Parties may otherwise agree."

It is also important to understand what the treaty does not do. The treaty is structured to provide only for the transfer of the physical assets of the Canal to Panama. It does not necessarily mandate the transfer of the Canal operation as a going concern with ongoing management structures and personnel systems. Thus, in order to ensure continuity in the Canal operation, the United States and Panama must create legal and policy structures to supplement the treaty.

According to U.S. law, the Panama Canal Commission, under the general supervision of its Board of Directors, is "responsible for the maintenance and operation" of the Canal. Presidential authority with respect to the Commission is exercised through the Secretary of Defense, who has delegated his responsibility to the Under Secretary of the Army. That designee is by law a member of the Board of Directors, along with the four other U.S. citizen members. Undersecretary of the Army Joseph Reeder is currently also Chairman of the Board of Directors.

The State Department has a special statutory role with regard to the transition of the Canal to Panamanian ownership and control. U.S. law provides that the U.S. Ambassador shall have "full responsibility for the coordination of the transfer" to Panama of those functions under the treaty and related agreements. Authority over the regular operation, management and maintenance of the Canal is the province of the Panama Canal Commission.

A Consultative Committee established by the treaty also has a role in making recommendations to the two governments concerning, among other things, transition issues. The part-time U.S. representatives to this committee rely on the State Department for staff work and coordination.

REVERSION OF MILITARY PROPERTIES

Article XIII of the Panama Canal Treaty provides that, when the treaty expires, the U.S. will transfer to Panama "without charges ... all rights, title and interest" we may have "with respect to all real property, including non-removable improvements thereon" that were used by the Panama Canal Commission or U.S. military forces. In other words, to the extent that the U.S. holds title or use rights to properties covered by the treaty, these rights will automatically transfer to the Panamanian government upon termination of the treaty.

Article XIII also contemplates the transfer of property before the treaty expires, giving us a wide degree of discretion regarding the timing of reversion. We also have considerable leeway on whether to leave removable USG property on defense sites being reverted or to remove such property.

The Panama Canal Treaty and related agreements contemplate that the United States will take measures to remove hazards to human life, health, and safety, and contain a number of specific provisions on that issue.

U.S. MILITARY PRESENCE

The Panama Canal Treaty gives the U.S. the primary responsibility to protect and defend the Canal until the treaty expires in 1999. This includes the right to station, train and move military forces within Panama. In the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal, which carries no expiration date, the U.S. and Panama agreed to maintain the Canal's permanent neutrality. As reflected in amendments and understandings added during the ratification process, this has been agreed by both governments to include the right of the U.S. to act unilaterally to meet any threat to the Canal, including the use of military force in Panama. But the Treaty, even as amended, does not include any right to base troops in Panama after 1999, absent a further agreement.

Article V of the Neutrality Treaty states that, after the termination of the Canal Treaty, only Panama shall maintain military forces within its territory. However, the U.S. instrument of ratification of the Neutrality Treaty includes specific language confirming that the Treaty would not prevent the two countries from making arrangements or agreements, including for the stationing of military forces or maintenance of defense sites, to fulfill their responsibility of maintaining the Canal's neutrality after 1999. The Panamanian government, in the bilateral "Protocol of Exchange" of instruments of ratification, expressly "agreed upon" the condition. As such, there is no treaty impediment to a new agreement to make possible a post-2000 U.S. military presence in Panama.

U.S. law concerning the Canal includes a sense of the Congress resolution expressing the view that "the best interests of the United States require that the President enter into negotiations with the Republic of Panama for the purpose of arranging for the stationing of United States military forces, after the termination" of the Canal treaty. This language, which reflected the view of the Congress in 1979, did not impose a binding legal obligation on the Executive Branch to enter into base negotiations. We are of course, attentive to the views of Congress on this matter and are prepared to consult as such views evolve.

THE SEPARATE ELEMENTS

THE CANAL

The overriding interest of the United States in Panama is the maintenance of a free and democratic government, coupled with an open economy to help bring prosperity and well being to Panama. The strategic United States interest in Panama is the efficient and secure operation of the Canal itself. Although the development of alternative intermodal routes for some commodities has reduced the importance of the Canal in trans-U.S. commerce, the Canal is still highly important to Japan, Chile, Ecuador and Peru, in addition to the United States. It is through this waterway that 13.4 percent of U.S. international shipborne commerce flows. Four percent of world trade passes through the Panama Canal annually. Flagged vessels from 78 countries used the Canal for a total of more than 12,000 crossings in 1994. It is important to the increasingly rapid flow of global commerce that the Canal be operated efficiently and reliably.

In the sophisticated management of the Canal, the confidence of user governments and shipping lines is paramount. If users believe that tolls will be raised excessively, that maintenance will be deferred or that delays on transit will increase, they will begin shifting their transport patterns. This in turn would reduce traffic and revenues, threatening the viability of the Canal. The Panama Canal Commission, which currently operates the Canal, maintains solid and regular communications with shippers. The Panamanian government has shown itself aware of the necessity to provide demonstrable assurances to users of the Canal. One response has been to create a Panama Canal Transition Commission, consisting of Panamanian nominees for the Board of Directors of the Panama Canal, Panamanian members of the Panama Canal Consultative Committee and two top Panamanian experts on the Canal. The Commission has begun to plan for a smooth transition of the Canal.

Another response is Panamanian government plans to organize and host a September 1997 Canal users' conference, with top levels of government and worldwide shipping in attendance. The idea is to acquaint Canal users in depth with Panamanian preparations to assume total management of the Canal. We believe this to be an excellent initiative and one which should bear positive results.

One of the first pieces of legislation passed by the new Panamanian Legislative Assembly last fall was a constitutional amendment setting the framework for an independent Panamanian Canal Authority. The amendment had been developed by the previous Endara Administration and passed by the previous legislature, but passage by two consecutive legislatures is required in the case of constitutional amendments. The Perez Balladares Administration threw its support to the amendment and engineered its passage. This continuity between two Panamanian administrations of opposing political parties reflects the broad consensus in Panama for responsible management of the Canal.

The constitutional amendment has positive features aimed at insulating the Canal organization from improper political influence and interference. However, it will be the details of the implementing legislation, and its subsequent interpretation and enforcement, which will determine the ultimate effectiveness of the new constitutional entity.

On March 9th, the U.S. Administration sent to the Congress proposed legislation to make changes to the Panama Canal Commission intended to facilitate a smooth transfer of the Canal to the Republic of Panama. This legislation was based on the recommendations that the President transmitted to the 103rd Congress in April of 1994. The changes are designed to anticipate the semi-autonomous, corporate type of successor organization which is contemplated by the constitutional amendment just enacted by the National Assembly of the Republic of Panama.

In the 1960's and 70's, the degree to which Panamanians were involved in operating the Canal became an issue. Now, however, it is indisputable that Panamanians are deeply and substantially involved in operating the Canal. Almost 90 percent of employees are Panamanian and over 40 percent of top management are of Panamanian nationality, including two of three section chiefs. The government of Panama now takes the position that continuity of management is more important than the nationality of Canal officials. We understand that consideration now is being given by the Panamanian government to make offers to senior Canal officials to stay on well after 1999, regardless of their citizenship, in the interest of retaining as many experienced hands as possible.

PROPERTY REVERSION

Between now and the end of 1999, the U.S. plans to return property comprising 77,000 acres and 4,272 buildings to the Government of Panama. Estimates of the value of land and improvements range upward from ten billion dollars. As Panamanians themselves have recently voiced in public debates concerning the process of property reversion, the optimum economic usage of these properties is essential to assure economic inputs as the U.S. economic presence is drawn down as the year 2000 approaches. U.S. bases inject \$450-500 million dollars into the Panamanian economy and create some thousands of jobs.

The record of Panamanian usage of already reverted facilities has been mixed. For example, facilities recently transferred such as the Curundu Heights Bachelor Officers' Quarters and the Coco Solo Hospital are successfully used and well-maintained by the GOP. The Panama Railroad and parts of Fort Gulick, transferred in 1979, are in partial or total disuse. However, the railroad was never economically viable without heavy subsidies, even before its transfer, and the Panamanian Defense Forces maintained Fort Gulick adequately until they were abolished following Operation Just Cause.

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We are encouraged by the attention currently being shown to the subject by the Panamanian government. Late last month, the Panamanian National Assembly passed an administration bill which revamped the structure of the Interoceanic Region Authority (ARI), intending to give the planning and execution of projects involving the reverted properties a new impulse.

Some Panamanians have expressed opposition to the legislatively-mandated changes, claiming that it means "politicization" of ARI. We prefer to wait to see how ARI moves ahead to deal with reverting properties, understanding that the Panamanian government envisages using privatization to the maximum extent possible. Experience has shown that grandiose government-managed projects often are expensive and cumbersome. All serious studies indicate that the only suitable disposition of the vast majority of the built-up areas is private development under applicable zoning, environmental and other regulations.

Canal users will be viewing Panamanian efforts to put reverted properties to productive use as they form their estimates of Panamanian competence to manage the Canal after 1999. Moreover, if the reverted areas are used in such a way as to increase growth, jobs and revenue to the government (perhaps with debt reduction as well), the temptation to use the Canal excessively as a source of income may be reduced.

For our part, U.S. officials will be working closely with Panamanians in a consultative relationship to plan and coordinate property return. This will be especially important on environmental aspects. It is of course up to Panama to decide how and for what purposes to use these properties. But we and the Panamanian people share a common interest in the sound use of the reverted areas. We believe this process of consultation will result in a smooth flow of returning properties and facilities in conditions which are environmentally sound and beneficial to the Panamanian economy, including the Canal.

CONSIDERATION OF A POST-2000 U.S. MILITARY PRESENCE

As I have already stated, U.S. policy is to comply fully with the Canal treaties. We are currently reviewing, not whether the treaties will receive full compliance, but how to structure our overall relationship with Panama so as to further our continuing interest in the Canal within the framework of the Treaties. Included in this review is the question of whether it would be in the U.S. interest to seek some form of post-2000 U.S. military presence in Panama. We are working closely with the Defense Department to address the issues involved.

We are looking at our Neutrality Treaty obligation to maintain the neutrality of the Canal and examining its implications. Together with DOD, we are reviewing the missions performed by the U.S. Southern Command in its area of responsibility and whether they require a forward presence in Panama. We are also looking at the implications in our relations with Panama and throughout the hemisphere of any possible decision to explore post-2000 basing with the Panamanian government.

The principal strategic interest in Panama, as I noted before, is the efficient and secure operation of the Panama Canal. Our responsibility to assure that the Canal remains open and secure to ships of all nations will not cease upon termination of the Panama Canal Treaty. As we are both obligated and allowed by the Neutrality Treaty to assure the Canal's protection, the question becomes whether a presence in Panama would significantly assist the U.S. in complying with this requirement. At the same time, we would need to consider what other U.S. objectives would be served by such a presence. Support for a strong counternarcotics role in the hemisphere could be one other such purpose. Training of U.S. troops is another, for example. An ideal jungle training facility exists at Fort Sherman, on the Atlantic side of the isthmus. There might be some advantage to Panama and other countries in the area to having U.S. forces available for search and rescue or other humanitarian missions as well. Consideration would also need to be given to the benefit of a forward military presence in the region.

As the USG looks at these possible benefits of a potential post-2000 U.S. military presence in Panama, countervailing considerations must be weighed as well. It would not do to spend large amounts of U.S. taxpayers money for expensive basing rights. That is something that the Department of Defense would have to weigh in the context of its overall program of base closings. Also, it would be important to judge whether such a presence would meet with major support from Panamanians in the future. Public opinion polls have been stable since 1991 in showing that about half the Panamanians think the U.S. should maintain about the same number of troops as now, while an additional 35 percent believe a presence should remain in "reduced" form. It may be the case, however, that the intensity of opinion is stronger among those opposed to a U.S. presence than among those who favor it. Opinion elsewhere in the hemisphere is at this point unknown but there might be broad acceptance of a U.S. military presence, particularly if Panama made clear that it wanted and accepted one.

RELATIONS WITH THE PANAMANIAN GOVERNMENT

The focus of this hearing is on the Canal and the U.S. military presence in Panama, but there was some concern expressed late last year that a political party founded by Omar Torrijos and later used by Noriega had come to power in the new Panamanian government. Let me address that.

Our relationship with the government of President Ernesto Perez Balladares is quite positive. The Panamanians have been extremely helpful to us on foreign policy matters of importance. President Perez Balladares stepped forward twice last summer in the face of Panamanian public opposition to offer safehaven to Haitian migrants and to actually provide safehaven for Cuban migrants for a six month period. We are grateful for the support. The Panamanian government also accepted Haitian General Cedras for asylum in Panama at a crucial moment, contributing to the restoration of democracy in Haiti.

President Perez Balladares, while drawing some Revolutionary Democratic Party stalwarts into the government, has also reached beyond the party for top talent. His Foreign Minister Gabriel Lewis Galindo, his Planning and Economic Policy minister Guillermo Chapman, and his Attorney General Jose Antonio Sosa are examples of the broad base of political talent in the Panamanian administration.

On the economic and financial fronts, we see the Panamanian government moving to close a Brady deal on debt, negotiating constructively with its commercial creditors. Panama is consulting on accession to World Trade Organization/GATT and lowering trade and tariff barriers in preparation for future trade negotiations. The USG is intensely interested in the rapid accession of Panama to the WTO/GATT and hopes that Panama will be able to continue with the type of economic adjustments that will position it for early full participation in the plan for trade expansion adopted at the Miami Summit of the Americas.

These moves to restructure the Panamanian economy are important for the U.S. for more than the usual good economic reasons. Panama, with 1.2 billion dollars in U.S. imports annually, is not a major export market for U.S. products, but there is an important relationship in our strategic interests between an economically healthy Panama and the Panama Canal. If, as Panamanian Planning Minister Chapman has pointed out, the economy is functioning well, it will provide a healthy economic environment within which the Canal can be administered. There will be less temptation for future governments to rely excessively on Canal revenues for the national budget -- risking loss of user confidence, traffic and ultimately the viability of the Canal itself.

An important element in our relations with the Panamanian government has been the fight against illegal narcotics and the proceeds derived from them. President Perez Balladares has moved quickly to set up an institutional framework within which money laundering can be detected and prosecuted. The Panamanian government is cooperating fully on the counternarcotics front with us and we look forward to positive results in the future.

RELATIONSHIP AMONG THE PANAMANIAN ELEMENTS

In conclusion, Mr. Chairman it is useful to view the elements of the future political, military and economic relationship with Panama as interrelated. The Canal requires an efficient and businesslike approach for its post-2000 operations, one which gives confidence to users and is insulated from political pressures or economic stress unrelated to the Canal business. The current Panamanian government is aware of these necessities and we are willing to work with them to create the structures and policies which will engender the confidence necessary to the continued viability of the Canal. The successful operation of the Canal will be more likely against a backdrop of a prospering Panamanian economy. The economy can be

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helped by optimum use of reverted military properties. The economy can also be helped by the restructuring and modernization now underway in the context of WTO negotiations and Panamanian anticipation of early negotiations toward a hemispheric free trade agreement. It is also possible, as one option which might be considered, that a limited U.S. troop presence in Panama would instill confidence in Canal users.

We will be considering these elements in the weeks ahead, Mr. Chairman, and once we in the Executive Branch have reached some preliminary conclusions, we would welcome consultations with the Congress, including with your Panel. We will of course be in touch with the Panamanian government to discuss the full panoply of issues with them at the appropriate time.

Thank you for the opportunity to present these issues to you. I look forward to responding to any questions you may have.

Mr. BATEMAN. Now, we will hear from Secretary Smith.

STATEMENT OF FREDERICK C. SMITH, PRINCIPAL DEPUTY ASSISTANT SECRETARY OF DEFENSE, INTERNATIONAL SECURITY AFFAIRS, DEPARTMENT OF DEFENSE; ACCOMPANIED BY BRIG. GEN. JOHN R. WALSH, ASSISTANT DEPUTY FOR POLITICAL MILITARY AFFAIRS, JOINT STAFF, J-5

Mr. SMITH. Mr. Chairman, members of the panel, it is a pleasure to be here this afternoon to discuss this important topic. With me are Brigadier General Walsh from the Joint Staff and other Pentagon experts to help answer your questions.

I would like to submit the entire text of my statement for the record and give a summary of the key points. The United States has important political, economic, and security interests in Latin America.

Our interests focus on helping to promote democracy, taking measures to increase economic growth and stability, combating the flow of drugs from the region to the United States, and in particular in Panama, defending the Panama Canal.

These are endearing interests that I believe will not change after the year 1999. The chief implementor of U.S. defense policy in Central and South America is the U.S. Southern Command. Its primary mission is to protect U.S. security interests in the region.

It accomplishes this mission by maintaining command and control of U.S. forces operating in the theater, defending the Panama Canal, supporting counter-drug efforts, strengthening professional military to military relationships in the region, and promoting peace and stability to enhance democratic development and economic growth. These military missions like our interests in the region will not change after 1999.

Current United States military strength station in Panama is approximately 8,800 personnel. The U.S. Atlantic Command maintains a regional presence contiguous to U.S. South Command's area of responsibility.

USACOM, that is the U.S. Atlantic Command, has command of nearly all U.S. based forces to use in fulfilling tasks in the hemisphere. These forces, together with those under the command of U.S. South Command are and will remain capable of responding to any threat in the region.

The Department of Defense is complying with the terms of the Panama Canal and neutrality treaties by transferring defense facilities to the Government of Panama and withdrawing United States forces.

The Panama Canal Treaty Implementation Plan signed by the Secretary of Defense in 1992, allows for the defense of the canal, continued support of counter-narcotics programs, use of training facilities for U.S. forces, emergency evacuation if necessary of U.S. citizens from the region, and humanitarian and disaster relief assistance.

In short, the plan fulfills treaty obligations while continuing to carry out the U.S. Southern Command missions. Our ability to carry out these missions will not cease upon the termination of the treaty.

In particular, under the protocol of the treaty concerning the permanent neutrality and operation of the Panama Canal which carries no expiration date, the United States will retain the right and responsibility to act against threats to the canal.

Secretary Perry has stated that while the United States will fully implement the terms of the treaties, we are willing to discuss the possibility of maintaining a U.S. presence in Panama after 1999 if the Panama Government believes, too, that is in its best interest.

The administration is conducting a thorough study of the requirements for a possible post-1999 presence in Panama. Participants in this study include the Department of State, the Department of Defense, the Joint Staff, U.S. South Command, OMB, the intelligence community, the National Security Council Staff, and the Panama Canal Commission.

The study includes requirements for maintaining a capable presence in the region, continuing to provide security of the canal, commanding and controlling forces deployed to the region, supporting counter-narcotics operations, ensuring adequate training facilities for U.S. forces, and staging for contingencies, search and rescue, humanitarian assistance, civic action, disaster relief and exercises.

These requirements, of course must be balanced with U.S. global interests, our overall force structure and basing structure in the post-1999 era, and limited fiscal resources. I want to emphasize that the review will include looking at three areas of major concern; defense of the canal, uninterrupted counter-drug support to United States and foreign law enforcement agencies, and maintaining the best possible training opportunities and facilities for U.S. military personnel.

We look forward to consulting with Members of Congress as we work through this difficult task. The situation in Panama in the coming years will present challenges and opportunities. The Department of Defense will comply with the terms of the Panama Canal Treaties.

At the same time, our regional interests will grow and our military forces will remain encased. Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Smith follows:]

Statement by
Frederick C. Smith
Principal Deputy Assistant Secretary of Defense
International Security Affairs

before the

Special Oversight Panel on the Merchant Marine
National Security Committee
House of Representatives

"Post-1999 U.S. Military Presence in Panama"

March 28, 1995

Mr. Chairman, members of the Special Panel, it is a pleasure to testify before your panel this afternoon to discuss U.S. interests in Panama and considerations for U.S. security involvement in Panama after the year 1999. Accompanying me from the Joint Staff is Brigadier General John R. Walsh, Assistant Deputy Director for Politico-Military Affairs. The Department of Defense is in full agreement with our colleague from the Department of State, Deputy Assistant Secretary Anne Patterson. We wish to associate ourselves fully with her statement.

In my statement I would like to discuss briefly (1) the enduring U.S. interests in Latin America and our defense policy for protecting those interests; (2) the mission of the U.S. Southern Command and our current force structure in the region; (3) implementation of the 1977 Panama Canal Treaties and related legislation; and (4) considerations for a post-1999 U.S. military presence in the region.

Regional Interests and U.S. Defense Policy

The United States has important political, economic, and socio-cultural interests in Latin America, many of which affect U.S. national security. While more serious strategic threats to U.S. national security abound in other regions, Latin America does not present any imminent strategic threat. After World War II, U.S. policy in the region was a constant of the Cold War in which local events were viewed geostrategically and often led to strained relationships with Latin American nations. The end of the Cold War has allowed us an opportunity to change our attitude and approach commensurate with the geographic and economic importance of the region.

Today, our security interests in Latin America focus on helping to promote democracy, taking measures to increase economic growth and stability, and combating the flow of drugs from the region to the United States. These interests derive from the region's proximity, its high standing as a trading partner, a shared commitment to democracy, the importance of the Panama Canal, and the cultural and family ties of Hispanic-Americans. Whenever possible, our strategy to pursue these interests looks to cooperative arrangements such as the North American Free Trade Agreement, the Summit of the Americas, the Organization of American States, and other multinational endeavors.

While Latin America is relatively free of armed conflict, tensions based on historical animosities remain. Contested borders, disputes over maritime boundaries, and refugee migration have the potential to spark regional conflicts. The current border conflict between Peru and Ecuador is an example of how situations can threaten regional stability. Cooperative engagement involving the U.S., international organizations, and Latin American nations should continue to pursue the goal of a definitive resolution of these long-standing issues.

The opening of the next century is likely to witness a more stable and dynamic Latin America where conflict resolution has been shifted to cooperative venues. Thus, Defense's role will be to remain engaged in bilateral and multilateral military-to-military and civil-military programs that build confidence and enhance cooperative regional security.

U.S. Southern Command and Current Force Presence

Much of the U.S. defense policy regarding the region is implemented by the U.S. Southern Command with its headquarters in Panama. The Command's primary mission is to protect U.S. interests in the region. It accomplishes this mission by:

- maintaining command, control, communications, and intelligence (C³I) to provide strategic and operational direction to U.S. forces operating in the theater;
- defending the Panama Canal and the area around the Canal;
- supporting counterdrug efforts;
- strengthening professional military-to-military relationships with regional armed forces to develop cooperative military postures and doctrine;
- promoting peace and stability to enhance democratic development and economic growth; and
- maintaining a high quality of life for U.S. forces and their families throughout the area of operations.

The Service components assigned to U.S. Southern Command are U.S. Army South, Ft Clayton, Panama; U.S. Atlantic Fleet, Norfolk VA (for planning purposes); U.S. Southern Air Force, Davis-Monthan Air Force Base, AZ; Special Operations Command, Albrook Air Force Station, Panama; and Marine Forces Atlantic, Camp Lejeune NC (for planning purposes).

Current U.S. military strength stationed in Panama is approximately 8,800 personnel. This includes personnel from the Army, Navy, Air Force, Marines, and Special Operations components and the USSOUTHCOM headquarters staff. They occupy 10 major defense sites and various isolated facilities totaling 77,000 acres. The current USSOUTHCOM drawdown plan calls for 5,650 military personnel on five major defense sites totaling 69,650 acres by the end of Fiscal Year 1998.

The U.S. Atlantic Command (USACOM) maintains a regional presence contiguous to USSOUTHCOM's area of responsibility. USACOM has command of nearly all U.S.-based forces to use in fulfilling tasks in the hemisphere; these forces together with those under the command of USSOUTHCOM are capable of responding to any threat in the region.

Treaty Implementation

The Department of Defense is complying with the terms of the Panama Canal and Neutrality Treaties by transferring Defense facilities and withdrawing U.S. forces. Transition activities are proceeding under the Panama Canal Treaty Implementation Plan, signed by the Secretary of Defense in 1992. This phased withdrawal allows for defense of the Canal, continued support for counter-narcotics programs, use of training facilities for U.S. forces, emergency evacuation, if necessary, of U.S. citizens from the region, and humanitarian and disaster relief assistance.

The issues of timing and costs of the withdrawal plan are reviewed on an annual basis, at which time the Commander in Chief of the U.S. Southern Command adjusts the plan and tasks the Service components to develop or modify supporting plans. The result is a treaty implementation plan that fulfills treaty obligations while continuing to carry out the U.S. Southern Command missions.

Our ability to carry out these missions will not cease upon the termination of the treaty. In particular, under the Protocol to the

Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal, which carries no expiration date, the United States will retain the right and responsibility to act against threats to the Canal.

Post-1999 Presence Considerations

Secretary Perry has stated that while the United States will fully implement the terms of the Treaties, we are willing to discuss the possibility of maintaining a U.S. military force presence in Panama after 1999 if the Panamanian government believes, too, that it is in its best interest. Indeed, there are indications in the negotiating history of the Treaties for assessing the needs for a possible presence.

In the Treaty Concerning the Permanent Neutrality and Operation of the Panama Canal, the U.S. and Panama agreed to maintain the Canal's permanent neutrality. Primarily due to reservations and understandings added by the U.S. Senate, both governments agreed that the U.S. has the right to act unilaterally to meet any threat to the Canal, including by use of U.S. military force in Panama. These reservations and understandings, however, do not include the right to base troops there after 1999 absent a further agreement.

Article V of the Neutrality Treaty states that after the termination of the Canal Treaty, only Panama shall maintain military forces within its territory. The U.S. instrument of ratification of the Neutrality Treaty, however, includes specific language adopted by Congress to confirm that the Treaty would not prevent the two countries from making arrangements or agreements, including for the stationing of military forces or maintenance of defense sites, to fulfill their responsibility of maintaining the Canal's neutrality after December 31, 1999. The Government of Panama, in the bilateral "Protocol of Exchange" of instruments of ratification expressly agreed to this understanding. As such, there is no treaty impediment to a mutually agreed post-1999 U.S. military presence in Panama.

Moreover, Section 1111 of the Panama Canal Act of 1979 includes a sense of Congress resolution declaring the "best interests of the United States require that the President enter into negotiations with the Republic of Panama for the purpose of arranging for the

stationing of United States military forces, after the termination of the Panama Canal Treaty of 1977...."

Given this background, an Interagency Working Group is conducting a thorough review of the requirements for possible post-1999 U.S. military presence in Panama.

The review includes requirements for maintaining a capable presence in the region, continuing to provide security of the Canal, commanding and controlling forces deployed to the region, supporting counternarcotics operations, ensuring adequate training facilities for U.S. forces, and staging for contingencies, search and rescue, humanitarian assistance, civic action, disaster relief, and exercises. These requirements, of course, must be balanced with U.S. global interests, our overall military force and basing structure in the post-1999 era, and limited fiscal resources.

I want to emphasize that the review will include looking at three areas of major concern:

- Defense of the Canal will remain a high regional priority. USSOUTHCOM could defend the Panama Canal against external threats with forces based in the United States. As stated in the Treaties, the Canal will remain neutral and the United States retains the right to use force in Panama to reopen the Canal or restore the operations of the Canal.
- The uninterrupted counterdrug support to U.S. and foreign law enforcement agencies is, and will remain, of major importance. Panama is located in the center of a major drug transit area and Howard Air Force Base provides secure staging for detection, monitoring, and intelligence collecting assets. The primary impact of not having a base in Panama will be on our ability to stage aircraft for counterdrug operations. Arrangements will have to be made so that operations are not hindered.
- Panama provides unique opportunities and facilities for training, such as the Jungle Operations Training Center and the Navy Small Craft Instruction and Technical Training School. When these sites in Panama are no longer available, they will be difficult to replicate elsewhere.

We will be challenged to accomplish the mission in a changing geopolitical environment. I, for one, am comforted by the words of

the Commander in Chief of the U.S. Southern Command who said in recent testimony, "...we have no vital military or economic interest directly at stake in Panama which we cannot support through some other strategy."

Conclusion

We should be optimistic about the future of U.S. regional security interests in Latin America. There are no immediate threats to vital U.S. security interests emanating from Latin America. Nevertheless, the area will require constant engagement because of the costs of the narcotics trade, mass migrations of refugees, likelihood of change in Cuba, persistence of low level insurgencies, and importance of unobstructed maritime transit rights, including via the Panama Canal.

The situation in Panama in the coming years will present challenges and opportunities. The Department of Defense will comply with the terms of the Panama Canal Treaties. At the same time, our regional interests will grow and our military forces will remain engaged.

Mr. BATEMAN. Thank you, Mr. Secretary.

The first question I have is as to whether or not any analysis has been done of the cost of maintaining the various military facilities that are on this inventory within the 77,000 acres and the 4,300 buildings in the context of the financial or fiscal resources of Panama to maintain them, to properly use them, and to direct them into productive use?

Has any such analysis been done?

Ms. PATTERSON. Mr. Chairman, an analysis is pending. They have a loan from the Inter-American Development Bank for \$8 million that would finance a study of that nature. It has been delayed. Panama lost a great deal of time under Noreaga and frankly not much has been done to conduct such a study so far.

Mr. BATEMAN. To date, some of the facilities have already been transferred. Am I correct?

Mr. SMITH. Yes, sir, that's correct.

Mr. BATEMAN. What has been our experience so far with those which have been transferred?

Ms. PATTERSON. Mr. Chairman, there were some facilities transferred in the late 1970's and the early 1980's, what used to be the old School of the Americas, the Panama Canal Railroad, and the Balball Port, I believe.

Those facilities are not in good shape. The old School of the Americas is frankly fully destroyed. But then it was used by the Panamanian defense force and it was destroyed in a firefight during Just Cause. The facilities we have transferred within the past couple of years, health clinic and I think some housing, have been well maintained and well used.

Mr. BATEMAN. The University of the Americas facilities, were they in reasonably good condition prior to the firefight that damaged them?

Ms. PATTERSON. Actually, they were used as a housing area and base by the Panamanian defense force. They had been recently well maintained. They were basically abandoned after Just Cause.

Mr. BATEMAN. The ongoing evaluation of defense security arrangements post-1999, how long will it be before the administration has determined what those arrangements should look like and what we should be seeking?

Ms. PATTERSON. We are anticipating that this will take us another few months. We are frankly already overdue to have the report done. So, we are trying to get it finished as quickly as possible.

Mr. BATEMAN. I welcome the fact that you said with candor that you feel like they are overdue. Alas, 1999 is not all that far away. You indicated a desire by the administration for consultation with the Congress.

Not much consultation can really be meaningful until the administration has a plan that it would want to share with us and hopefully seek our support on, and which certainly ought to be evaluated on a totally bipartisan basis. First, it seems to me we need to know where we want to go and then work together to see how is the best way to get there.

Mr. Taylor, you have questions.

Mr. TAYLOR. Thank you, Mr. Chairman.

I am going to take issue with your remarks about the School of the Americas. I think very little of the damage that I saw was the result of Just Cause. Almost all of the damage that I saw was the result of looting.

Ms. PATTERSON. Oh, yes, it has been abandoned.

Mr. TAYLOR. The only thing left was the door.

Ms. PATTERSON. Yes. They are not using it. I, too, have seen it. It was basically abandoned after the Just Cause. It has not been maintained. I did not wish to imply that—they have not restored it. It was just left.

Mr. BATEMAN. If I might interject, I did get the impression, perhaps erroneously from what you said, that it had been very severely damaged as a result of the fire. . . .

Ms. PATTERSON. It had been damaged. Then it was basically abandoned. Nothing has been done to maintain it since that time.

Mr. BATEMAN. But the real problem with the property was not the fire, but that after the fire it was abandoned and not maintained.

Ms. PATTERSON. It was unused and parts of it had been destroyed; both things.

Mr. BATEMAN. Excuse me, Mr. Taylor, proceed.

Mr. TAYLOR. I am curious as to where, and I will open this up to the panel, where the administration is in the process of renegotiating, should there be a decision on the part of our administration, the Congress and the Panamanians to try to keep some of these installations, with the key words being, if I am not mistaken, in the area immediately around Fort Amador some revert this year, this calendar year.

That there is nothing in the DOD budget to maintain them after that point. In going to some of the questions that Mr. Bateman had to a previous panel, there is for all of the American installations a roadmap of installations and a day that they are turned over to the Panamanians.

The DOD with limited defense dollars on those things that are going to be turned over have slowed down maintenance and in some instances stopped maintenance and certainly not planning or budgeting any funds for maintaining them after the days when they revert. Is that not correct?

The question is, if there is going to be a change in our policy, given the knowledge that we have that anything that is left to fend for itself even for a short period of time, I'm talking about just months, if it is left to fend for itself, it won't be there to take back over should we and the Panamanians change our minds about keeping it.

What is being done along those lines so that this is done in an orderly and legal manner, should we decide to keep some of these installations, and should our Panamanian host decide to let us stay?

Mr. SMITH. Mr. Taylor, in general, in response to your question, it is not until 1998 that we would turn over any of the facilities that we contemplate that we might want to have access to or continue using for some purpose. The many facilities have already been turned over as we have stated. Amador, I believe, is scheduled for this year, as you have stated.

Mr. TAYLOR. But didn't in February the Panamanian Government say they would consider an extension for Amador because they just weren't ready to take it over yet? Isn't that correct? What is the decision with regard to that in particular?

Mr. SMITH. Not to our understanding.

Mr. TAYLOR. It was in the paper. It was in the Panamanian paper in February.

Mr. SMITH. We will check on that, but not to our understanding. We will check.

Mr. BATEMAN. Let me interject this. Mr. Secretary, either or both, it is critically important to this panel that we have as quickly as you can get it to us, the inventory of all of these facilities, the time lines already agreed to for transfer.

Ms. PATTERSON. I think we have got that. I'll bet we have that with us.

Mr. SMITH. Yes, we have that.

Mr. BATEMAN. I want more than just a list of facilities and dates. I want information as to what is planned or contemplated either by us or the Panamanian Government for these properties not become wasted, so to speak.

Not necessarily here in a public hearing, but perhaps after I have had a chance to see that list, perhaps we might visit and discuss the current state of the administration's thinking and as importantly the thinking of the Panamanian authorities as to whether or not these time lines, adjustments, and arrangement should in the mutual interest of the parties be reevaluated.

Mr. TAYLOR. Mr. Chairman, may I?

Mr. BATEMAN. Just briefly.

Mr. TAYLOR. Mr. Smith, I am here not to try to harass you, but just having seen what happened at the School of the Americas, I am not painting worse case scenarios. I have seen what happened to installations that were turned over and they are just a concrete shell now.

Housing is a key issue throughout the military, throughout the world. In the case of Amador, we have some of the better housing that is available for our military personnel. It is well maintained. It is due to revert this year.

The Panamanians have offered to let us stay, I think, at least for a year. The question that immediately comes to mind is, if it is our decision to stay and if there is housing that has already been paid for by the American taxpayer that is in fairly good shape, if not really good shape, wouldn't it make sense to move quickly if it is the policy of this country and the policy of the Panamanian nation to let us stay to try to take care of what we have rather than letting it revert and have the DOD to come to this committee in a couple of years saying we need some money for housing in Panama to replace what we have lost because the right hand wasn't talking to the left?

Mr. SMITH. Yes, in principal, I agree with you on that. I just said that, in general, according to our plan, the way it is laid out is 1998 is the crossover point where the major facilities that we would be interested in are scheduled to be transferred.

Mr. TAYLOR. May I have a followup question, Mr. Chairman.

Mr. BATEMAN. Let me help you with that. I didn't hear an answer to the question about the specific facility that is slated for transfer this year.

Ms. PATTERSON. Mr. Chairman, Mr. Taylor is talking about Fort Amador.

Mr. BATEMAN. Yes.

Ms. PATTERSON. We have with us the head of the Treaty Implementation Office. They have very carefully laid out a scenario that would involve giving properties back gradually and maintaining those properties under any conceivable scenario that we would wish to maintain it in the post-2000 period. Correct me if I am wrong, but it is my understanding that under none of these scenarios would Fort Amador be retained.

Mr. TAYLOR. May I ask a followup then?

Mr. BATEMAN. Sure.

Mr. TAYLOR. At those installations that South Command and other DOD representatives are interested in retaining with hopefully the permission of the Panamanians after the treaty time, is there adequate housing there at the installations you plan on keeping and hopefully can keep, to take care of the people that will be stationed there or will you be coming back to us in a couple of years saying well, the bases we kept didn't have enough housing and therefore we need some more money for housing?

It would make a heck of a lot more sense to be thinking about that in advance and hopefully dealing with our Panamanian friends in advance to keep those things we need for all of our needs.

Mr. SMITH. Without knowing the exact force structure that we might want to retain there we of course don't know the housing requirements. In general, we believe that yes, there will be adequate housing should we work out arrangements for post-1999.

Ms. PATTERSON. Mr. Taylor, nothing has been a higher priority with both General Joulwan and General McCaffrey who is the current commander of Southern Command. I have seen their briefings on this several times. The access to housing and sufficiency of housing has been a very high priority for them. I think any plan they will come to in 1998 has taken that into account.

Mr. BATEMAN. Permit me to say, Secretary Smith, you sound more like the State Department than Ms. Patterson does, this afternoon. Your answers do not bring much information. We want the details. We want it as to Fort Amador which apparently is very, very eminently going to be transferred.

We would like to look at it. As the saying goes, the devil is in the detail. We want some detail. Don't think you will be bothering us with detail. We do seek it. We do want it. We will try to be constructive in our use of it.

Mr. TAYLOR. If I may close on that issue, Mr. Chairman?

Mr. BATEMAN. Yes.

Mr. TAYLOR. Mr. Smith, Ms. Patterson, I know in private conversations that I have had with high ranking military officials of our Nation, they have a number in mind of how many Americans they would like to have there if it is our wishes and the wishes of the Government of Panama. They already know that number.

My question for you is, should it be of mutual consent between our nations that this happen, are you making adequate preparation to hang onto those things that we have already paid for so that given a very limited and very static DOD budget that you are not coming back to us in a year or two saying, oops, we let that one go and we need x number of billion dollars to be building some housing down in Panama?

I am afraid this committee, with base closings going on all around this country, it is not going to be very favorable in its reaction. I will just leave it at that. Brigadier General, if you would like to comment on that.

General WALSH. I would, Mr. Taylor. It is a good point. General McCaffrey has done a superb job based on that number that you just talked about in ensuring that all of the facilities that are required to support that force structure, to include all of the quality of life requirements are kept on-hand under U.S. control until a decision is made in the analysis.

Mr. TAYLOR. Thank you very much. That's what I was hoping to hear.

Mr. BATEMAN. Might you share with the committee General McCaffrey's plan or recommendation?

Mr. SMITH. Excuse me, Mr. Chairman, the question?

Mr. BATEMAN. The question was, since General McCaffrey of the Southern Command has come to a recommendation as to the dimensions and the nature of their need, could you share with us that plan?

Ms. PATTERSON. Mr. Chairman, we would be happy to share it with your staff. I would much say I would rather do it in private. It is basically an internal document of the U.S. Government, internal recommendation to the Secretary of Defense.

Mr. BATEMAN. I can take that point.

Ms. PATTERSON. We will be happy to do so, of course.

Mr. BATEMAN. With the firm understanding that this is not something that I would regard as something for the public arena or for the public record.

Ms. PATTERSON. No. It is basically a recommendation, an input to our internal study right now, but of course we would be happy to share it with you at your convenience.

Mr. BATEMAN. The committee necessarily is going to be involved in the authorization bills and the funding streams that go with all of these arrangements. We don't want to be surprised. We want to be in the loop. We want to be very constructive.

We need information. I think this is a critical piece of the information to be properly used as an internal document not for public disclosure.

Ms. PATTERSON. Certainly.

Mr. BATEMAN. Mr. Longley is next.

Mr. LONGLEY. Mr. Chairman, I would just make a short statement. I am in the process, obviously, as a new member learning quite a bit about this. Listening to the comments of the ranking member and the chairman, and given the time line that we are on, I guess I would like to reemphasize the importance of the points that they have tried to make. I think we need to make some critical decisions here and make sure that our plans have been developed

so that whatever happens after 1999 we are in a position to execute it on most favorable terms. Thank you, Mr. Chairman.

Mr. BATEMAN. Thank you, Mr. Longley. Mr. Abercrombie, the gentleman from Hawaii.

Mr. ABERCROMBIE. Mr. Chairman, Mr. Taylor covered my concerns. I just want to note by way of emphasis that I think the housing question is very important. As you know, on the National Security Committee as a whole the housing question is one that has to be dealt with.

We want to try and come to a final conclusion on it. We don't want to get into a situation where we start a kind of competition on it.

Mr. BATEMAN. Thank you, Mr. Abercrombie.

Do we have any further questions?

I believe that's it, but we look forward to, while you were sharing with us, the information we requested. If you could do it before the panel makes its visitation to Panama which I think we leave something like April 25 or 26, it certainly would be helpful.

Ms. PATTERSON. Certainly, Mr. Chairman.

Mr. BATEMAN. If we have that, I think it makes our visit much more meaningful as we see that which there is to be seen.

Ms. PATTERSON. Certainly.

Mr. BATEMAN. Thank you very much. We appreciate your being here with us today.

At this time it is my pleasure to welcome the next panel of witnesses. We have Adm. Albert H. Herberger, the Maritime Administrator. We are happy to have him before the panel and look forward to his testimony.

We also have as a witness this afternoon, Adm. Philip M. Quast who is commander of the Military Sealift Command. We think it is more than appropriate that the two of you be sharing the committee table this afternoon because of your obvious common interest in our maritime security.

Admiral Herberger, we look forward to hearing from you.

STATEMENT OF ADM. ALBERT H. HERBERGER, MARITIME ADMINISTRATOR

Admiral HERBERGER. Thank you, Mr. Chairman.

Mr. Chairman, and members of the panel, I am pleased to appear before you to discuss the Maritime Administration's fiscal 1996 authorization request. I request that my prepared statement be placed in the record. I would like to make some overview remarks regarding the thrust of our overall program this year.

Mr. BATEMAN. That will be done. You may proceed as you choose.

Admiral HERBERGER. Our objectives in the fiscal 1996 program are to first ensure an active fleet of U.S. privately owned and operated commercial vessels to preserve a U.S. industrial shipbuilding and supplier base; ensure a pool of trained U.S. citizen mariners; also, to enhance efficient port and intermodel systems, and to maintain a reserve fleet of cargo vessels to be used in time of national emergency or humanitarian emergencies.

I would like to specifically talk to parts of our program that support each of those five major areas. To ensure the active fleet, we are proposing a maritime security program to maintain U.S. pres-

ence in our international trade and to provide sealift and skilled mariners in time of national need.

This maritime security program is a 10-year program. It would support up to 50 ships. It would cost over the 10 years, \$1.1 billion per year over the 10 years. It would consist of militarily useful, modern vessels. It would also incorporate a new emergency preparedness program to take advantage of the modern capacity of the U.S. companies' intermodel system terminal operations and vast infrastructure.

This private sector infrastructure is about 8.5 billion dollars' worth of terminals and equipment. It is our vision that we should be capable of using that system, both in peacetime for all of the economic advantage, as well as being able to use it in time of a national emergency in support of deployed forces or for whatever other purposes we would need it.

In the area of preserving an industrial shipbuilding and supply base, there is a five part program that came online a year and a half ago. In the centerpiece of that is the Federal Loan Guarantee Program, the title XI program, which guarantees private sector loans for commercial shipbuilding in the United States.

Currently, we have \$85 million available. This supports 850 million dollars' worth of shipbuilding activity. If we succeed in getting a legislative change to change the subsidy rate, we could even increase that to as much as 1.3 to 1.5 billion dollars' worth of shipbuilding activity.

We have today, 1.5 billion dollars' worth of pending applications for guarantees and another list, a secondary list, that is another \$1.8 billion of what we will call today, reasonably potential projects.

This includes both shipbuilding modernization, shipyard modernization and improvements, as well as programs for export vessels, as well as domestic.

Mr. BATEMAN. Excuse me. What was that last figure of reasonably promising?

Admiral HERBERGER. The last figure was \$1.8 billion; a list of 1.8 billion dollars' worth of potentially reasonable projects.

There has been some recent criticism of the title XI program regarding defaults; the majority of which took place in the mid-1980's. I would just like to state at this time that this program has been in existence for 40 years. It has supported 16 billion dollars' worth of projects, the building of 9,000 vessels and hundreds of thousands of jobs during this period.

For 37 of the 40 years the program generated a positive cash flow. There have been no defaults on approval since 1985. When you take into consideration when a vessel is put in default, we retain the vessel. We sell it. We recoup some of the money plus the fees that have been paid into it.

Our estimate is that of the defaults which amount to \$2.7 billion over the total 40 years, the true cost to the Government is about \$400 million; about a 3-percent loss which is very competitive in any sector.

I think it has been represented as concentrating purely on the defaults. Most of them took place from 1983 to 1987 when the energy sector was hit very hard and there was a general recession

that impacted on the barge. It is a good news story. We need to keep the story straight in terms of the impact of this program.

The next area is to ensure a pool of trained citizen mariners. Kings Point and the State maritime academies graduate the finest best educated to provide the safest and most efficient operation in the marine industry.

We must maintain a base of highly skilled mariners if we are going to be prepared to maintain a capability to ban, not only the Government fleet which is getting larger year by year, but also the commercial fleet.

At a time when the world at large is concerned with the quality of mariners in general, and when there has been a series, almost a continual series of marine accidents, wherein in the investigation it has come back to the human factor, this is not the time to be looking at closing down or reducing the impact of our particular educational base.

This applies not only to Kings Point, and the State academies, but also to the very fine facilities that the maritime unions, the labor unions, provide. We do have the best mariners in the world.

Today there is a shortage of 200,000 licensed mariners worldwide. There are predictions by studies that there will be a shortage of 400,000 by the year 2000. This is not the time to be taking actions to reduce the capability that we have when we are out on the point, if you will, to ensure that the rest of the world are coming up to the high standards of our shipping operations.

We have a very serious obligation, I think, to ensure that we maintain this capability. Enhance sufficient port and intermodel systems, the ports are the centerpiece of the intermodel infrastructure.

Ocean transportation has been the centerpiece of a revolution in transportation that has benefited the whole world and particularly the interior of the United States. There are farmers and manufacturers today that are shipping products well beyond any distance that they ever envisioned when they started farming, if you will.

It is all brought about by the investment of technology in modern intermodel systems, containers, double stacked trains and all of those things that have come on the line, all of which have been brought about by the U.S. companies maintaining that foothold and they are leading the world and the world is copying that.

I think it is very important that we continue to put attention on the port areas to continue to develop the efficient intermodel activity in the ports to ensure that we have land and water access to the ports. Also, in time of national lead, to coordinate the military and Defense Department use of these very fine facilities to save, again, the Defense Department from having to out and replicate that type of capability.

The next area, the fifth area, is to maintain the reserve fleet, the Ready Reserve Force [RRF] which is a part of the National Defense Reserve Fleet. We have learned the hard way, if you will, from the lessons learned in Desert Storm and Desert Shield that in order to maintain the right level of readiness, you have be sure that you do that and you don't go penny-wise and dollar-foolish on it.

We have, since the Desert Storm and Desert Shield, those lessons were well learned. There has been a cooperative effort be-

tween the Defense Department and the Department of Transportation.

I can sit here today and say the readiness has improved. We need to keep working on it. We do need a level of support in order to do that. As an example of its use, 51 vessels have been activated since 1992 for Haiti, Somalia, and other types of regional humanitarian activities. We have vessels today that are out in an operational status.

Starting in fiscal year 1996, the RRF budget funds would come out of the defense budget. The Maritime Administration would continue to manage the RRF fleet, and it is for one simple reason.

We have been doing it for the better part of 36-odd years. We have all of the experience needed to maintain commercial ships, given the proper resources, in a high state of readiness to be available when the military sealift command, transportation command needs them.

One other item that I would like to mention at this time. It is a part of our authorization proposal. It is that we need a support to continue MARAD's authorization to issue war-risk insurance.

As an example, it is called title XII. Just as an example, during Desert Storm, we were able to respond to the needs to issue war-risk insurance. A conservative estimate is that there was a cost avoidance for DOD of something on the order of \$436 million by us being able to issue war risk insurance in time of need. This is a continuation of the authorization which runs out on June 30.

Mr. Chairman, I look forward to working with the members of your panel in all of these important areas. I am ready to respond to any questions that you may have.

[The prepared statement of Admiral Herberger follows:]

STATEMENT
OF
ALBERT J. HERBERGER
MARITIME ADMINISTRATOR
ON
BEHALF OF
THE
MARITIME ADMINISTRATION
BEFORE THE
SPECIAL OVERSIGHT PANEL ON
THE MERCHANT MARINE
OF THE
COMMITTEE ON NATIONAL SECURITY
U.S. HOUSE OF REPRESENTATIVES
IN SUPPORT OF
FISCAL YEAR 1996 AUTHORIZATION
FOR THE
MARITIME ADMINISTRATION
MARCH 28, 1995

DEPARTMENT OF TRANSPORTATION
STATEMENT OF THE MARITIME ADMINISTRATOR
ALBERT J. HERBERGER
BEFORE THE SPECIAL OVERSIGHT PANEL ON
THE MERCHANT MARINE
OF THE
COMMITTEE ON NATIONAL SECURITY
U.S. HOUSE OF REPRESENTATIVES
IN SUPPORT OF FISCAL YEAR 1996 AUTHORIZATION
FOR THE MARITIME ADMINISTRATION

Mr. Chairman and Members of the Subcommittee:

I welcome the opportunity to be with you today, to discuss the Maritime Administration's (MARAD) budget request for Fiscal Year 1996.

The Maritime Administration's authorization request recognizes the military and economic value of having a fleet of private commercial vessels owned by American citizens, crewed by American civilian

seafarers, and operated in compliance with American safety and environmental standards. It also recognizes the importance of the American shipbuilding industry by furthering the objectives of the National Shipbuilding Initiative, contained in the National Shipbuilding and Conversion Act of 1993, which seeks to strengthen that industry through the Title XI loan guarantee program.

National Security

American ships and American seafarers have always come through for us during times of war or national emergency. Just this past year, we celebrated the outstanding role the merchant marine played in World War II with President Clinton's visit aboard the Liberty Ship, S.S. JEREMIAH O'BRIEN, off the coast of Normandy on June 6th. The merchant marine also served in Korea and Vietnam, and more recently, American seafarers and American ships served with honor in support of our armed forces in the Persian Gulf, Somalia and Haiti.

Our national military strategy is facilitated by the two complementary strategic concepts of overseas presence and power projection. In order

to remain engaged globally with fewer U.S. forces permanently stationed overseas, we must proportionately increase our capabilities to project forces abroad. This requires airlift and sealift, and the commercial U.S.-flag fleet is a cost-effective source of sealift for resupply of our armed forces and sustainment of our capabilities overseas. The commercial fleet complements the Maritime Administration's Ready Reserve Force and the Department of Defense's organic fleet, which enable U.S. forces to be rapidly deployed overseas in an emergency.

Economic Security

A modern U.S. merchant fleet also supports a strong U.S. presence in international trade. Without your continued support for U.S.-flag operations, the United States will become wholly dependent on foreign-flag ships to carry its exports and imports. We will not be able to negotiate from strength with our trading partners. Furthermore, the United States will lose an effective voice at the International Maritime Organization (IMO), for without a U.S.-flag fleet, we cannot effectively influence the setting of worldwide shipping standards.

In recent years, there has been dramatic change in the efficiency and productivity of ocean and intermodal transportation, and the prime innovators have been our American carriers. They have pioneered specialized ships, containerization, double stack rail cars, specialized containers, electronic equipment identification, satellite tracking and just-in-time, door-to-door services which reduce inventory and warehousing costs for American industry. The American public, as consumers of imports and producers of exports, greatly benefit from this efficient and expanding intermodal system.

Maritime Security Program

Mr. Chairman and Subcommittee members, I will now discuss the Maritime Administration's authorization request. It includes \$175 million as the initial funding for a new ten-year Maritime Security Program (MSP). Under the draft "Maritime Security Act of 1995", which the Administration has transmitted separately, we will be able to maintain a U.S.-flag maritime fleet of up to 50 modern, efficient liner vessels crewed by skilled U.S. mariners. Ship operators participating in

the MSP must agree to make their ships and entire intermodal transportation systems available for sealift support during war or national emergency. This partnership with the commercial community will provide the government with cost-effective sealift utilizing existing assets as a complement to the DOD sealift programs and the Ready Reserve Force. Furthermore, the Department of Defense can use the carriers' vessels and intermodal transportation systems for door-to-door transport of equipment and supplies for the armed forces. Maintaining this fleet will also allow us to retain a pool of U.S.-citizen crews that will be available to crew the vessels in the Ready Reserve Force and the Department of Defense's organic fleet during times of emergency.

The MSP is essentially the same ten-year program that was proposed by the Administration last year, but the funding source is completely different. It is proposed that the MSP be funded as part of the Department of Transportation budget and not from increased tonnage duties as proposed last year. Payments to U.S.-flag ship operators engaged in foreign trade would not exceed \$2.5 million annually for FY 1996 through 1998, and would be reduced to \$2 million annually for

FY 1999 through 2005. These payments would be about one-third less than the current operating-differential subsidy program, thus giving operators built-in incentives to reduce their operating costs. The Maritime Security Act would also substantially deregulate the maritime industry by relaxing existing restrictions on vessel acquisitions, trade routes, and foreign vessel operations.

Enactment of an MSP cannot come too soon. Just last month, MARAD granted Sea-Land Service, Inc., permission to transfer five containerships to Marshall Islands registry, and Lykes Bros. Steamship Co. permission to time charter four new foreign-built containerships under foreign registry. In November 1994, MARAD granted permission for American President Lines, Ltd. (APL), to operate six new foreign-built ships under foreign registry. These companies have indicated their strong support for enactment of the Maritime Security Act and are committed to participation in the MSP.

America's future as a maritime superpower is at stake. This year will make or break what remains of our U.S.-flag presence on the high

seas. Without a maritime reform bill, in all likelihood, for the first time in modern American history, our U.S.-flag presence in international trade will vanish, along with our civilian sealift support, seafaring jobs and the technological leadership of our American carriers.

I will now briefly outline the remainder of the Administration's budget request.

Maritime Loan Guarantee (Title XI) Program

The Administration's budget request for fiscal year 1996 includes \$48 million for Title XI loan guarantees. An additional \$4 million is included for administrative expenses. This request supports the National Shipbuilding Initiative (NSI), and could enable MARAD to guarantee private sector loans to build ships and strengthen America's shipyards of up to \$1 billion, assuming proposed legislation to increase the Title XI guarantee fee is enacted.

The Title XI loan guarantee program allows MARAD to guarantee private sector debt financing for the construction or reconstruction in U.S. shipyards of U.S.-flag vessels and export (foreign-flag) vessels, and U.S. shipyard modernization and improvement projects. Title XI loan guarantees enable ship owners and shipyards to borrow funds from the private market on terms that may not otherwise be available, at a fixed rate, with longer term maturities.

Since enactment of the National Shipbuilding Initiative by Congress fourteen months ago, we are seeing tangible results of our commitment to a vital shipbuilding industry and to the thousands of skilled workers who are part of it. Interest in this initiative from both domestic and foreign buyers has been strong, and includes recent approval of the first U.S.-built commercial ship order for a foreign buyer in over 35 years. We are putting U.S. shipyards and U.S. shipyard workers back to work, and making our shipyards competitive internationally once again in commercial shipbuilding. Foreign buyers and investors are coming back to U.S. shipyards. The FY 1996 authorization and

appropriations request is essential to continue our support for the U.S. shipbuilding industry.

So far, in FY 1994 and 1995, MARAD has approved fourteen new applications totalling over \$600 million in financing. These projects include MARAD's approval of the application of Fleves Shipping Corporation, for \$133 million in loan guarantees for financing of the first ocean-going vessels for export built in the United States in over 35 years. These tankers will be built in Newport News, Virginia, and are expected to generate 500 shipyard jobs.

On February 7, 1995, I announced the approval of more than \$160 million in new loan guarantees which includes a \$134 million guarantee for United States construction of the first four double-hull product tankers that will meet the requirements of the Oil Pollution Act of 1990.

MARAD has also approved the issuance of loan guarantees for shipyard modernization projects of \$22.7 million at the National Steel and

Shipbuilding Company (NASSCO) in San Diego, California and \$18 million at Avondale Shipyards in Louisiana. Other applications for shipyard modernization projects are now under review. These modernization projects will allow shipyards to build ships more efficiently and at less cost, resulting in more competitive commercial facilities.

As of February 27, 1995, MARAD was reviewing 19 applications for \$1.5 billion in loan guarantees.

In an effort to make the Title XI loan guarantee program even more effective, the Department has recently proposed legislation to increase the guarantee fee provisions of the Title XI loan guarantee program. These provisions apply to obligations for both U.S.-flag and foreign-flag vessels, and U.S. shipyard modernization and improvement projects under the Title XI program.

The proposed amendments would require an obligor to make a lump sum payment of the increased guarantee fee at the time of closing of

the loan guarantee obligation. Such a requirement will lower the risk to the Government by ensuring that it receives the full guarantee fee due for the entire term of the obligation, and will also encourage loan guarantee applicants to enhance the financial structure of their transactions in order to qualify for the lowest possible guarantee fee.

Ready Reserve Force (RRF)

The President's Budget proposes to fund the National Defense Reserve Fleet, including the Ready Reserve Force (RRF), from the National Defense Sealift fund in the Department of Defense beginning in fiscal year 1996. Management of the RRF will remain with the Maritime Administration. The necessary authorization will be included in the Department of Defense (DOD) authorization bill. The RRF consists of 92 ships kept in a high state of readiness to enable them to be activated in 4, 10, 20 or 30 days to meet military sealift requirements in the event of a war or national emergency. In addition to providing sealift to the U.S. military during Operations Desert Shield and Desert Storm, the RRF has supported worldwide peacekeeping and

humanitarian efforts, such as those for Somalia and Haiti.

Management of the RRF is governed by a Memorandum of Agreement (MOA) between the Department of Transportation and the Department of Defense.

Operating-Differential Subsidies (ODS)

The new Maritime Security Program will replace the existing operating-differential subsidy (ODS) program with a more flexible and cost-effective program. However, we still have obligations to fulfill under the old program for a few more years. To support these obligations under the existing ODS program, the Administration is requesting \$162.6 million. ODS contracts for liner vessels will remain in force until 1998; all bulk vessel contracts will expire by 2001. In fiscal year 1996, we expect to pay ODS contract obligations for 35 liner vessels and 19 bulk ships.

The requested amount is a net decrease of \$51.7 million from the FY : 1995 Congressional appropriation of \$214.3 million due to the decrease in the number of subsidized vessels projected for FY 1996.

Operations and Training (O & T)

An authorization of \$81.6 million is requested for Operations and Training, including \$42,973,000 for Maritime Education and Training and \$38,677,000 for operating program expenses.

The maritime education and training program reflects the cost of officer training at the U.S. Merchant Marine Academy at Kings Point, New York, and Federal financial support to the six State maritime schools operated by California, Maine, Massachusetts, New York, Michigan and Texas. Supplemental training courses in shipboard firefighting, marine diesel engineering and national defense-related courses for licensed and unlicensed merchant mariners are also funded from this account.

The U.S. Merchant Marine Academy at Kings Point offers a four-year undergraduate, full scholarship program which leads to a Bachelor of Science degree and to a merchant marine license as Third Mate or Third Assistant Engineer, or both. In addition, the students are enrolled as midshipmen in the U.S. Naval Reserve and are commissioned upon graduation as ensigns in the U.S. Naval Reserve with an eight-year obligation. Graduates of Kings Point and the State maritime academies are the foundation of our efforts to ensure the American maritime labor force is the best educated, safest and most responsible in the world. At the same time, we must maintain a continuous renewal of highly qualified entry level officers in the civilian merchant marine, so that we are prepared to crew sealift ships quickly in a crisis. These young professionals give us that assurance.

The State maritime academies program assists states in the education and training of individuals for service in the U.S. merchant marine. Assistance is in the form of direct payments to the academies, incentive payments to cadets, and maintenance and repair of five ships on loan for use as training ships.

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The Additional Training account funds MARAD headquarters personnel services for the U.S. and State academies, and the costs of developing and maintaining current data on the maritime labor force.

Expenses for maritime training at the Merchant Marine Academy at Kings Point are budgeted at \$32,063,000; expenses for financial assistance to State maritime academies are budgeted at \$9,325,000; and expenses for necessary additional training are budgeted at \$1,585,000.

Operations program expenses include the ports and intermodal development programs that are essential segments of the Department's overall program and the plan for a seamless transportation system. These programs are integral to improving America's competitiveness in foreign trade and services while, at the same time, being responsive to the need for industrial redevelopment and a sound ecology. National defense experts are agreed that intermodalism and port readiness are the keystones of modern military logistics. Lack of capability in these areas could reduce the efficiency of any future projection of force.

Examples of intermodal/ports projects are: (1) the Cargo Handling Cooperative Program, a government/industry cost-shared program that enables commercial and defense industries to benefit from new technologies to increase competitiveness; (2) the Rail/Marine Intermodal project to examine U.S. technology needed in the year 2000 to create an efficient infrastructure for the 21st century; and (3) the Mid-American System Study to develop a strategic plan for utilization of inland waterways, thereby strengthening U.S. industry, agriculture, foreign trade, domestic employment, and ecology. These are a few of the efforts that are national in scope, leveraged with the private sector, and beneficial to the economy in many magnitudes beyond the minimal expenditure.

Operations program expenses also include research and development, operating programs and general administrative costs. This program reflects costs incurred by headquarters and region staff in the administration and direction of the various programs established to fulfill MARAD responsibilities. This program also provides for

coordination of U.S. maritime industry activities under emergency conditions.

In FY 1996, \$4,977,000 is requested for research and development and cost-shared cooperative programs with the maritime industry to assess innovative technology to improve competitiveness, intermodal transportation, maritime safety, environmental protection, shipyard revitalization and national security. Through these dollars we expect to leverage three times as much from the industry.

Summary

In summary, the Maritime Administration's FY 1996 budget request reflects the President's commitment to preserving the maritime industry of the United States and maintaining the United States as a maritime nation.

Our budget maintains funding for sealift readiness and the continuation of a U.S.-flag fleet, shipbuilding initiatives, maritime education and training, and maritime support programs.

This concludes my prepared statement. I will be pleased to answer any questions you may have.

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Mr. BATEMAN. Thank you very much, Admiral Herberger.

We appreciate your testimony. I am sure we will have some questions. At this point, we will turn to Admiral Quast for his testimony. Welcome Admiral.

STATEMENT OF ADM. PHILIP M. QUAST, COMMANDER OF THE MILITARY SEALIFT COMMAND

Admiral QUAST. Thank you for this opportunity, Mr. Chairman and members of the oversight panel.

I appreciate the opportunity to come before you to express my support for the President's fiscal year 1996 budget, that portion dealing with the sealift readiness; especially the readiness of our Ready Reserve Force which is a critical resource for this Nation's surge sealift capability.

I ask that my written statement, as well, be included as a part of the hearings.

Mr. BATEMAN. It will be.

Admiral QUAST. I have been in and out of the building with some frequency lately in an effort to highlight for several members of the panel the importance of sealift to our national security.

Before addressing the RRF readiness, which is my major concern, I would like to say a little bit about the Military Sealift Command [MSC] and where we fit in the sealift picture.

The Military Sealift Command operates for the purpose of fulfilling three vital global missions. The first is to move all of the Department of Defense's cargo that goes by sea. That includes petroleum.

Second, we provide combat ready logistics forces for our Navy fleets around the world.

Third, we provide reliable special mission ships that provide services to various agencies in the national security arena. On any given day there are more than 130 MSC ships. Today, we have 136 fulfilling these three missions providing what we in the transportation business refer to as logistics from the sea.

Sealift continues to grow and it is important to our Nation's security. During Desert Storm, 95 percent of the logistics to support that contingency came by sea. Again, during the past fiscal year, events have demonstrated that sealift gives our military forces the capability to deploy forward indefinitely if necessary.

Clearly, the recent events in the Caribbean have reaffirmed this important aspect of national security, once again, particularly with respect to the Ready Reserve Force.

During the past summer we had to gear up for numerous operations in the Caribbean which included migrant processing, Operation Sea Signal and Able Vigil, and finally the operation which returned President Aristee to Haiti, Operation Uphold Democracy.

A dozen of the roll-on, roll-off ships, these are the RO/RO's, one barge carrier, and a crane ship were activated from the RRF on very short notice to respond to this contingency. These ships were activated, loaded and headed south to Haiti in just a matter of a few days.

Because no one knew for certain whether U.S. intervention would be forcible or peaceful, we had to essentially load two types

of armies, one for a nonopposed operation and one for a forcible entry contingency.

This amounts to two separate and different armies for this one operation. Subsequently, the RRF ships and their crews provided the vital supplies that enabled United States forces in Haiti to operate smoothly as they continue to do today.

Uphold Democracy was what we call a textbook surge sealift operation which provided immediate transportation of heavy military on RRF RO/RO ships to the scene of action, Port-au-Prince.

They were uniquely suited for the poor harbor conditions that we found in that Haitian port. They were able to offload military equipment speedily in an environment of austere port conditions and infrastructure.

Despite the unforeseen nature of the operations, we responded with the speed and proficiency that have become our national sealift hallmark.

Uphold Democracy reaffirmed once more that 95 percent of all military equipment and supplies needed to support any contingency must be transported by sea. Key to our supremacy in sea logistics is having the optimum readiness in surge sealift.

Following the sealift support of U.S. forces deployed to the Persian Gulf during Desert Storm, Congress mandated a mobility requirement study which gave credence to the great importance that surge sealift had during mobilization.

The original MRS [mobility requirement study], most recently the MRS Bottom-Up Review which I understand was signed just yesterday, recognized the need for additional surge sealift and established the requirement for 10 million square feet of surge sealift capacity be done by the end of this century.

Today, we are half way to that goal. We have slept which is why the approval of the President's budget request for the RRF is necessary to bring us closer to fulfill the MRS requirements.

Because the RRF is a primary source of surge sealift for rapid response in times of crisis, the recommendations coming from that study, the MRS study that this force be beefed up to include a total of 36 RO/RO ships is a needed goal that we are slowing down on, but we need your help.

In order to reach that goal, 19 additional RO/RO ships were required. MARAD proceeded to buy 12 of those 19 in fiscal year 1993, which brought the total up to 29 of the goal of 36. Just last month MARAD purchased two additional RO/RO's which will be overhauled in U.S. shipyards and join the force next year.

However, we still have shortages, five RO/RO shortages that we need to fill. Despite the projected sealift growth in the coming years, the Ready Reserve Force experienced funding setbacks within this current fiscal year and cuts that have slowed the pace for acquisition and lowered our readiness have occurred. The RRF funding problem contributed to the 5 million square foot shortage of the goal of 10 million square feet. The \$100 million cut in maintenance funding for this RRF fund caused both DOD and DOT to have to transfer 13 of the RRF ships to the National Defense Reserve Fleet, and to lower the readiness level of 29 RRF ships and reduce 29 other RRF ships to a 30-day readiness, which essentially puts it out of the surge.

These actions resulted in a 1.7-million-square-foot reduction in readily available RRF surge sealift capacity. In the early surge sealift, this is the equivalent of about one heavy division during an initial deployment.

A loss of this dimension is significant and hinders our sealift posture. With a shortage of U.S. commercial ships with the appropriate DOD specifications needed during wartime, it is important to remember that the RRF compensates significantly for the shortfall of military useful private sector ships.

These are the RO/RO ships. They are the most critical valuable ships to the military. They are the most effective source of military sealift and make an important military action possible and timely.

The RRF program can be put on track in meeting the MRS requirement once again if the President's fiscal year 1996 budget request is approved. Now is a critical time for your most serious consideration and support of this readiness issue.

We must continue to focus on this shortfall in the surge as outlined in the MRS study and close the gap in readiness as quickly as we possibly can.

Time is of the essence. Today, we are only half way to that goal. We need your support of the Ready Reserve Force to ensure that we continue to acquire and maintain the capability to support the Nation's national military strategy.

Thank you for the opportunity to appear before the panel and I am ready to answer any questions you may have, sir.

[The prepared statement of Admiral Quast follows:]

NOT FOR PUBLICATION
UNTIL RELEASED BY THE
SPECIAL OVERSIGHT PANEL
ON THE MERCHANT MARINE

STATEMENT FOR THE RECORD
VADM PHILIP QUAST
COMMANDER
MILITARY SEALIFT COMMAND
BEFORE THE SPECIAL OVERSIGHT PANEL
ON THE
MERCHANT MARINE
HOUSE NATIONAL SECURITY COMMITTEE

NOT FOR PUBLICATION
UNTIL RELEASED BY THE
SPECIAL OVERSIGHT PANEL
ON THE MERCHANT MARINE

***Vice Admiral Philip M. Quast, USN
Commander
Military Sealift Command***

Vice Admiral Phil Quast, a native of Sheboygan, Wis., was commissioned an ensign in the U.S. Naval Reserve in 1961. His initial assignment was aboard USS MATTHEWS (AKA 96) where he served as a Boat Group Commander.



A variety of seagoing assignments followed: Navigator aboard USS KING (DLG 10); Weapons Officer aboard USS TWINING (DD 940); Commander, River Patrol Division 532, Vietnam, and Executive Officer, USS TALBOT (DEG 4). He was the Commanding Officer of USS BENJAMIN STODDERT (DDG 22) (1978-1981) and the Commissioning Commanding Officer of USS BUNKER HILL (CG 52), (July 1985 to April 1988). While on BUNKER HILL's initial Western Pacific deployment, he served as Commander of the Battleship MISSOURI Battle Group supporting U.S. flag tanker transits through the Straits of Hormuz. During Operation Desert Storm, as Commander, Cruiser-Destroyer Group Three, he commanded the Nimitz Battle Group.

Vice Admiral Quast's shore assignments include: Instructor of Naval Science at the California Maritime Academy; Personnel Program Officer of the Commander, Cruiser-Destroyer Force, U.S. Atlantic Fleet; Instructor of Weapons System Engineering and Battalion Officer for the Brigade of Midshipmen at the U.S. Naval Academy and Junior Officer Assignment Branch Head, Bureau of Naval Personnel.

Vice Admiral Quast's initial flag officer assignment was as Head of the Assignment Division, Naval Military Personnel Command in 1988. He then served on the staff of the Chief of Naval Operations, as Director, Total Force Programming/Manpower Division and as Director, Military Personnel Policy Division. Vice Admiral Quast's most recent assignment was as Director, Surface Warfare Division, Chief of Naval Operations staff.

Vice Admiral Quast's personal decorations include: the Legion of Merit with three Gold Stars in lieu of subsequent awards; Bronze Star with Combat "V" and one Gold Star; Meritorious Service Medal and the Navy Commendation Medal. Vice Admiral Quast was the first recipient of the Admiral James Stockdale Leadership Award for the Pacific Fleet in recognition of his performance as the Commanding Officer of USS BENJAMIN STODDERT.

Vice Admiral Quast holds a Bachelor of Science Degree from Carroll College in Waukesha, Wis., and a Masters Degree from Marymount College (Virginia). He is a graduate of the Armed Forces Staff College, the Naval War College (Staff Course) and the National Defense University.

Vice Admiral Quast is married to the former Peggy Lord of Santa Barbara, Calif., and they have a family of five children.

Good afternoon Mr. Chairman and Members of the Panel. I am VADM Philip Quast, Commander of the Military Sealift Command. It is a pleasure to have the opportunity to appear before you today to discuss the FY 1996 authorization for the U.S. Maritime Administration.

Mission

The Military Sealift Command has three missions which are global in nature. MSC provides efficient sea transportation; combat ready logistics forces; and reliable special mission ships for the Department of Defense in peace and war.

The sea transportation part of our mission is accomplished as the Navy Component Commander for the United States Transportation Command. Strategic Sealift assets are used for this purpose.

Strategy

DoD requirements for strategic sealift can be broken down into three components, prepositioning, surge and sustainment. Prepositioning provides for deterrence and initial rapid response in the event of a

contingency. Surge sealift involves the immediate transportation of heavy military equipment from the continental United States, using specialized roll-on roll-off vessels, to the theater of operations.

Sustainment sealift follows and keeps our forces armed, fed and supplied relying primarily on commercial intermodal liner service. All of these strategies have been employed during the current fiscal year (FY95).

The Ready Reserve Force, or RRF, is utilized to meet our requirements in all three areas. Currently there are 10 RRF ships being utilized for prepositioning. Eight are being employed in the AWR-3 (Army War Reserve Afloat) program, in an interim capacity, until replaced by new construction and conversion Large Medium Speed RO/ROs (LMSRs) and two are tankers capable of delivering fuel from 4 miles offshore over undeveloped beaches. To fulfill part of our surge sealift requirement the RRF contains 22 roll on/roll off ships in a four-day readiness status for the purpose of rapidly loading heavy Army and USMC wheeled and tracked vehicles. Twenty nine ships are maintained in a 10 to 20-day readiness status to meet

other aspects of the surge requirement such as the Afloat Follow on Echelon (AFOE) for the Marine Corps and the Combat Logistics Force (CLF) for the Navy. The remaining 29 ships are maintained in a 30-day readiness due to underfunding of RRF O&M in FY95.

Recent Operations

Prior to last year's Congressional cuts in the Maritime Administration's budget, the Ready Reserve Force was at the highest state of readiness ever. This was a result of the intensive management efforts by DoT and DoD since the Gulf War. We continue to drive towards increasing their reliability. Ready Reserve Force ships have had a critical role assigned in recent operations. In Operation Vigilant Warrior eight RRF ships were in active status in prepositioned squadrons and were sent to the Persian Gulf. Although two of the eight ships had casualties during the deployment and two had casualties following cargo discharge, these casualties did not significantly impact on their ability to perform as directed. While these casualties did not adversely impact our operations they are naturally of concern. I would prefer to maintain

these ships at an even higher level of readiness and I have taken steps to make that happen. In Operation Uphold Democracy 14 RRF ships were activated in support of humanitarian operations for Haiti. Thirteen of these ships completed their missions without major incident.

Ready Reserve Force Funding

Today the RRF, the most cost effective source of surge sealift, coupled with our 8 Fast Sealift Ships, represents our predominant source of surge sealift capability. In FY95, RRF O&M funding, which was a part of the Department of Transportation (DoT) funding process, was reduced by \$100 million from the President's budget of \$250 million for O&M. This forced us to make significant changes in force size, maintenance, and readiness status in order to focus limited funds on our most capable and critical ships. Specifically, while maintaining our 22 RO/RO ships at 4-day readiness, we reduced the readiness and maintenance on 29 other high priority vessels, placed an additional 29 vessels in a minimal-maintenance 30-

day readiness status, and transferred 13 vessels to the National Defense Reserve Fleet.

Additionally in FY94, \$158 million of prior years appropriations, available for purchase of additional RO/RO ships to meet the goals of the congressionally mandated Mobility Requirements Study was rescinded. Two RO/RO ships destined for the RRF are currently under contract with the \$43 million appropriated to DoD in 1995. We still need to acquire approximately 5 more RO/ROs for the RRF to meet the DoD's goal of 36 RO/RO ships.

These funding shortfalls have resulted in degradation to our near-term capability to deploy forces rapidly and could cause a significant delay in responding to a major regional contingency. This year RRF O&M and acquisition funding became DoD budget items. This shift of funding responsibility to DoD, especially in the light of strategic lift's high priority in our overall defense program, ensures RRF funding can be appropriately and sufficiently considered by the Congressional committees having oversight of defense related programs. For FY 96 we

are requesting \$289 million for RRF O&M funding and \$70 million for RRF RO/RO acquisition funding. This request is included in the National Defense Sealift Fund (NDSF). These funds will go a long way toward restoring our strategic lift capability which was adversely impacted during FY95. In the outyears we need to ensure that the RRF continues to receive an equivalent level of O&M funding. In addition to the \$70 million in RRF acquisition funding for FY96 we estimate a requirement for an additional total of \$105 million between FY97 and FY98 to complete the acquisition of the last required RRF RO/ROs.

Maritime Security Program

While we pursue the essential readiness and modernization of our organic sealift fleet, we have not forgotten the importance of the U.S. maritime industry to our overall sealift capabilities. Just as we did in the Gulf War, in Somalia, and more recently back to the Persian Gulf, we rely extensively on our commercial partners to support our worldwide intermodal transportation requirements. In peacetime we ship over 16 million tons of DoD cargo using privately owned U.S.

flag ships crewed by U.S. merchant mariners, spending over \$1.7 billion annually within the maritime industry. In wartime we depend upon the commercial maritime industry to support the flow of sustainment and ammunition cargoes and to provide the mariners necessary to crew our organic ships.

To ensure continued availability of this critical capability, I support the proposal for a Maritime Security Program (MSP) funded by DoT. I must emphasize that the MSP is not a substitute for the unique military capabilities provided by the RRF and the Navy's Large Medium Speed RO/RO acquisition program, which are specifically designed for the afloat prepositioning and rapid deployment of the full range of military equipment.

Merchant Mariner Availability

Increased productivity of modern containerships has resulted in shrinking numbers of seafarers in the commercial seagoing industry. In a worst case scenario, when trying to crew DoD surge sealift ships rapidly in a crisis, this reduced availability of U.S. mariners may in the future, impact the activation of

surge sealift. We are initiating a working group to determine the feasibility of meeting our merchant mariner requirements through non-traditional sources if so required during a future contingency. Some of the alternatives to be reviewed include, mariners from the inland waterways, the Great Lakes, domestic offshore industries; possible modifications to the obligation of graduates from the U.S. Merchant Marine Academy and perhaps the establishment of a Naval reserve program. We hope to be able to report out on the results on this study later this year. An initiative in the House of Representatives of the 103rd Congress that I would like to see become reality is Merchant Mariners Reemployment rights. This would provide Merchant Mariners with substantially equivalent job protections afforded our military reserve personnel. It would make it possible for qualified merchant mariners to volunteer to crew our RRF vessels and other vessels chartered by DoD without fear of losing their jobs when they return to their civilian employers. Such a measure is necessary and prudent to improve the availability of merchant seaman during a time of crisis.

Summary

In summary, I would like to state that the cuts in the FY 95 RRF budget hurt the strategic sealift program. The RRF is a critical component of our strategic sealift force, comprising 75% of today's organic surge capability and will still represent over 50% of our surge sealift requirement when the final program is in place. We need your support of the Ready Reserve Force to ensure that we acquire and maintain the capability to support the United States National Military Strategy.

Mr. BATEMAN. Thank you very much, Admiral Quast.

I don't expect either of you could say this, but one of the nice things I guess about being chairman is that I can say this. The Vice President's reinvention of Government working documents with respect to maritime affairs of this Nation is virtually a disaster.

If implemented, as some of the people involved in that study have suggested, we wouldn't have an American shipbuilding industry. We wouldn't have an American flag merchant marine. We wouldn't have any American maritime manning capability to meet our national security requirements into the future.

I am delighted, Admiral Herberger, to hear the positive testimony that you have made as to what the Maritime Administration does, what it needs and why its needs need to be met; both in terms of how critical it is to our national security that we have a merchant marine and that we have a corps of maritime sailors who are prepared to meet the Nation's needs in the future and the shipyards in which we can maintain our national security requirements.

These are the three problems with the maritime community. I am glad that you have addressed them. Hopefully, working together, we will see that we continue to focus on these needs and that we do make all of the Members of Congress that this is a maritime nation and that we have no power unless we remain a maritime power.

That it doesn't come free. That it is a national security concern and we must be and remain very sensitive to it. I am glad that you gave us information with respect to the need for continued training of maritime personnel.

I want you to repeat in case I misunderstood it, that data you shared with us about, did I hear a 200,000 requirement in terms of the international maritime community?

Admiral QUAST. Today, there is a shortage of 200,000 licensed mariners. The prediction, because of the training rate, the worldwide training that, that shortage could be as high as 400,000.

You would have to triple the current worldwide training rate to provide the sufficient mariners. The concern is, is that in recent years, there has been a source of sailors coming again, mostly from the underdeveloped areas that are not fully trained and as well educated.

There has just been a series of maritime disasters that when the survey or the study is completed, it comes back to the human element. We are losing in terms of the worldwide capability of mariners.

The United States for so many years, certainly in the mid-1930's, when so much of our maritime training support started, it was primarily driven by the fact that there was this critical shortage of highly qualified people.

The Merchant Marine Act of 1936, that was the—the *Moral Castle* disaster and there were other maritime industry accidents. We were having the same type of phenomena now worldwide with just the series of what are becoming catastrophic because of the size of the vessel and the impact it has on the environment as well as human lives.

There is something like 300 mariners that have been lost at sea in the last 5 years. In this day and age, that is unconscionable, but it is due to the low quality. The United States has been in the lead. We have been at all of the IMO conferences, driving the standards up and now would be not the time to give up being a flag nation and just become a port nation.

Mr. ABERCROMBIE. Mr. Chairman, would you yield very briefly?

Mr. BATEMAN. Very briefly.

Mr. ABERCROMBIE. Thank you. I just want to make sure I understand. So, in other words, what we are facing right now then is increasing competition from foreign sources with increasingly unqualified people on the ships from those foreign sources as compared to the standards we are now maintaining in the United States. Is that a correct statement?

Admiral QUAST. Ninety-five percent of our commerce comes into the U.S. ports in foreign vessels. There is a significant percent of the foreign vessels worldwide that are considered substandard. There is a lot of activity in recent years to begin to take action. International Maritime Organization, our Coast Guard, and others are beginning to take significant action to try to weed out those substandard vessels.

I am not saying that all of the foreign vessels that come in have—

Mr. ABERCROMBIE. I am speaking about the crews now.

Admiral QUAST. I am talking about the crews. That's right. When you look at the series of maritime disasters in recent years worldwide, you will find that in 85 percent of the cases, it is not mechanical failure, it is human error.

Mr. ABERCROMBIE. Then over and above exhortation we have no power to increase the standards or the measurement of those standards.

Admiral QUAST. We participate in the International Maritime Organization and are very effective in bringing about a higher standard. I want to be sure that you don't misunderstand.

Mr. BATEMAN. The gentleman from Mississippi, Mr. Taylor.

Mr. TAYLOR. Thank you, Mr. Chairman.

I am curious if either of the admirals could provide for the record, when you said 95 percent of the supplies that went to the Persian Gulf war went by sea, what percentage of that was on either U.S. Government-owned or U.S.-flag vessels?

Admiral QUAST. I will have to take that for the record. I don't know the exact percentage.

Admiral HERBERGER. I do and I am not trying to one-up my friend here—85 percent of the dry cargo, of the dry cargo, not the POL, went by ship—15 percent went by air. Of the total amount of dry cargo, 20 percent was carried by foreign-flag vessels under charter for that particular engagement. So, 80 percent of that dry cargo went in by U.S. Government-owned or commercial vessels that had U.S. mariners as crews.

Mr. TAYLOR. What about your POL?

Admiral HERBERGER. The POL, again, I think whenever you add POL to that dry cargo, then you come up to the 95 percent goes by sea.

Mr. TAYLOR. What percentage of the POL was U.S. flag or U.S. Government?

Admiral HERBERGER. We would have to get back to you on that. Because of the nature of being in that particular area, much of the POL source came from the Middle East. It was unique really in our experience. I don't know the statistics on what percent went on U.S. flag versus foreign.

Mr. BATEMAN. If the gentleman would yield briefly to followup on the point that I think needs to be made.

Mr. TAYLOR. Sure.

Mr. BATEMAN. In the Persian Gulf, you had one of the most comprehensive broadbased alliances or coalitions that has ever been brought to bear in a conflict. We aren't always that fortunate in having that broader base coalition.

While we could utilize non-U.S. resources in some significant measure during Operation Desert Storm/Desert Shield doesn't necessarily mean that we will always be able to do that in other conflicts which may arise where the alliance or the cohesiveness of the alliance is less adequate. Is that a fair comment?

Admiral HERBERGER. That's my assessment, Mr. Chairman.

Mr. BATEMAN. Go ahead, Mr. Taylor.

Mr. TAYLOR. Thank you, Mr. Chairman.

Admiral Quast, a few weeks back we had the opportunity to talk about a couple of issues one of which was the question of the SL-7's being available while RO/RO ships were being purchased overseas. The alternative that was proposed by several of us from shipbuilding regions of the country was that since there is a glut of RO/RO's in the international market and they are not getting much for leasing them, why did you not lease RO/RO's and then turn around and build some here in order to maintain the Navy's shipbuilding base or use the SL-7's while you built some here?

Again, what was the thought behind going out and purchasing foreign, especially at a time when I think this year's defense budget has a minuscule number of new starts as far as shipbuilding is concerned?

Admiral QUAST. Sir, first of all, we are already chartering two of the U.S. flag RO/RO's. There are very few U.S. flag RO/RO's left in the inventory; a handful; maybe 5 or 6. As far as purchasing RO/RO's with MARAD's assistance, we are trying to meet the requirement as set forth in the mobility requirement study.

As I indicated in my statement, we are only at 50 percent of that requirement. Time is critical to us and we are trying to fulfill particularly the RO/RO's, the ones that MARAD keeps in ROS-4, the highest state of readiness in our RRF fleet. We are trying to get that number up to the 36 that have been outlined and required by the mobility requirement study.

If we were to build, as you suggest, (a) it wouldn't get us a ship in the near-term. We are talking probably several years; and (b) the cost would probably be a whole lot more than the Department of Defense's budget has put against it, which is in the upcoming budget, \$70 million for purchase of RO/RO's.

Mr. TAYLOR. Admiral Herberger, I think it is your testimony, in the conclusion of it, you mentioned you wanted to do some things

that would maintain our Nation as a maritime nation. You don't use the word "power." You used maritime nation.

Pardon me, but don't you think this Nation deserves better than that? I have been on this committee for 6 years. I saw a Republican administration, with all due respect to my Chairman who I know his heart is otherwise, that basically said, in fact, I even heard from old Rob Ortell who is on the administration's payroll saying in effect, we don't need American ships if we can lease them overseas cheaper. I had hoped for better from a Democratic administration. I am disappointed that you don't want the ship to sink on your watch. That your goal apparently is just to slow down the rate of sinking.

I would like both of you gentlemen to respond to that. I think we can do better as a Nation. I think we have to do better as a Nation.

Otherwise, the people who come after you with a lot of gold on their sleeves are going to be coming to this committee saying, well the Israelis make a nice destroyer, we may want to buy one there and the Japanese make a nice destroyer. We are not going to have an industrial base.

Why is there a reluctance on the part of the people whose job it is to look out for the maritime interest of this Nation to be so utterly unambitious? You just happen to be sitting here. If someone else was sitting there, I would ask them the question.

Mr. BATEMAN. I can assure you that he is not picking on you personally.

Admiral HERBERGER. Mr. Congressman, I would very much desire to have the United States be a maritime power. What we are attempting to do at this particular time and what the administration has been trying to do for the last year and a half, 2 years is to revitalize and get some action going in these areas, and to step back to a much larger program. At this particular time, the resources needed, the time needed, but by the time we could get the support to get a start, we would lose what we have.

I am not saying that our program is a transition, but we absolutely have to stop the hemorrhaging. We absolutely have to permit our shipyards to get back into some commercial shipbuilding and therefore we think our approach at this time is modest, I agree, but with all of the other pressures that are being brought to bear on the Federal budget, what we have attempted to do is fashion a multifaceted program to maintain a presence in shipbuilding and commercial shipbuilding as well.

It is not leading us back to being a world power in these areas. I don't know what the future holds. We may, because of the introduction of our technology and other circumstances that are beyond our control, get back. I don't think we are going to get back to the post-World War II period where we were by far the largest maritime nation, both in shipbuilding and size of fleet.

The challenge here, I think, is that our U.S. companies have introduced the world class technology which has revolutionized transportation. Even though the fleet is not as large, the productivity we are getting out of that fleet is significant. A good example is you take the 1965 fleet, we are 76 percent smaller, but we have a 21-

percent greater productivity out of the fleet we have today. That is due to the application of technology.

I would like to see us a maritime power again. Our effort is a balance, with all of the other considerations having to do with the budget impact, to ensure that before much more time passes we hold on to the core of the good things that we have before we lose them. That is about my only answer at this stage.

Mr. TAYLOR. Admiral, let's refresh each other's memories. Two years ago this committee, under the leadership of Mr. Dellums, with a great deal of help from our Republican colleagues and Mr. Johnson sitting next to me, Bill Anderhasey drafted the title XI revitalization program.

I am a Democrat, but I will say publicly the Democratic White House got in our way every chance they could. First, they tried to kill it. Then to try to minimize it. Then the President, God bless him, calls a press conference and claims credit for the whole thing when they let out some contracts.

Mr. BATEMAN. The gentleman's recollection is very good.

Mr. TAYLOR. We haven't been saying, OK, title XI is working, people are applying for loans and we have a good record, other than the offshore supply boats, which this committee never should have signed off on, but I don't think any of us were here then. I am not going to point the finger at anyone who certainly wasn't here.

Rather than saying, it is working, let's expand it, you say let's grow it incrementally, but let's increase the upfront cost to any potential user of this which we both know is going to discourage them.

Then third, we are hearing from those people who are interested that the American yards desperately want a 25-year loan guarantee program to go out and market in the world market, yet the administration says, oh, no, if we do that, some of our foreign competitors who happened to have signed off with other international agreements with us would be angry.

Admiral, those people are subsidizing these shipyards. Those people, in the case of Japan, are already building over 300 merchant ships a year. Where within our Government are those people, who are paid what I think are decent salaries by the taxpayers of this country; is someone going to stand up and say, let's look out for this country?

Let's look out for the approximately 100,000 people working in the shipyards and all of the related industries like the Bear Bags Morris Industry over in Wisconsin, the Joint Diesel in the Midwest, the steelmills in Pennsylvania, on down the line.

I would think the two people who ought to be championing that cause are sitting at this table and both of them have the first name of Admiral. If the President was here, I would be saying the same to him. I'm sorry he is not here and you have got to be the whipping boy. At some place, it has got to go on record.

Admiral HERBERGER. Again, I think what we are proposing—we have been out of commercial shipbuilding for quite some time; in some cases 15 to 18 years. The yards in the Far East have got that kind of a lead. They have been concentrating on each yard builds a single ship. They are very good at it.

Between Korea and Japan they probably have 67 to 70 percent of the world orders in those particular type vessels. We happen to be entering a period now when there is going to be a worldwide need for 7,000 to 9,000 oceangoing vessels in the next 10 years.

We see this as an opportunity for the United States to get back in and try to gather in a percent of that. If we got 1 percent of it, it would be 70 ships a year. On a conservative side, 90. If we got 3 percent it would be 270 ships.

When you look at the condition of our yards and their capability to build commercial ships competitively today without a huge Government support program, the program that we are approaching, we think, is pragmatic and realistic within the budget concerns. I wish it could be more, but that is not the kind of support that we see available with all of the other requirements placed on the Federal budget this year.

Mr. TAYLOR. Two short questions.

What is your agency's attitude toward an 87 percent unguaranteed? What is your agency's attitude toward 25 years?

Admiral HERBERGER. Yes, absolutely. Those are the things that are making it work today.

Mr. TAYLOR. But why the recommendation to raise the upfront cost of the potential buyer, with the understanding that the only types of ships that we are funding are those with a military usefulness. Should, God forbid, they come back to this country, they become an addition to our fleet. That is the whole purpose in title XI. We do have that included in the title XI program.

Admiral HERBERGER. Title XI is being used in support of shipbuilding primarily. There are other types of vessels that are not militarily useful that are being covered by title XI, just as they have been in the historic past.

There are some significant vessels that would be useful, product tankers, but they will be foreign owned. The export program, the particular program in the Newport News yard is for 40,000-ton product tankers, a new design that Newport News has come up with.

They will be owned and operated by a Greek shipping company. I am not saying that they wouldn't be available in time of an emergency, but when we expanded the reach of that program, in order to jump start some shipbuilding, we got into some other areas, which is helping us get back into some shipbuilding and hopefully these incremental starts will lead to more capability and a greater number of orders, to become more competitive in the world market. Again, we have got to walk before we can run again. The competition is keen. We have a particular window of opportunity to get back into some shipbuilding.

Mr. BATEMAN. If I might, let me interject some observations here.

Mr. TAYLOR. Sure.

Mr. BATEMAN. The title XI program as it has benefited the shipbuilders of Newport News has been up to date; the program that made foreign merchant marine acquisitions possible. I can assure you that my shipbuilders at Newport News would be even more pleased to build product carriers for American-flag operations.

To date the title XI that has paid off in terms of encouraging domestic American shipbuilding has been what was made available for ships being constructed for export. To the extent that succeeds and the product carriers get built, the learning curve improves the productivity of the work force, hopefully there will come a time when American ship operators will be ordering product carriers for their fleets in American shipyards instead of this constant pressure upon them.

If they are going to modernize their fleets, to do it in foreign shipyards. Let me make this comment about the change in the title XI upfront cost that Mr. Taylor made reference to. I personally don't have a position on that to this point. What we are going to have to do is to make sure that the tradeoff on leveraging the amount of ship construction money that you can get for x dollars of loan guarantees is not offset by making the financing so attractive that no one any longer wants it and ships won't get built.

It is a delicate line. We will look at it and certainly want to discuss with you our thoughts on it as it develops. Clearly, we will consider the legislative initiative without any comment on my part that it now stands endorsed or damned. We will look at it.

I think you will appreciate the fact that there is a point where you can meet yourself coming back if you increase the leverage so much that the terms become unattractive and therefore unutilized.

Admiral HERBERGER. Mr. Chairman, we have had since the beginning of the title XI program a fee and it is 0.5 to 1 percent. Depending on the outstanding balance each year, and it is dependent on the risk factor of the particular loan as you would in any banking or financial.

What we are asking for is a range increase. It is now 0.5 to 1. We want it from 0.75 to 1.5. It would vary depending on the creditability of the given loan. Those fees are put into a special fund that would be there to cover defaults.

By reducing the risk to the Government we will be able to lower the 9.98 subsidy rate we use now down to 7.2 or 5.5, getting 50 percent or 100 percent more coverage by the program. The other benefit that we have in this thing is that if we have an 87.5 percent loan, that means that the applicant pays 12.5 percent.

This upfront fee would be part of that fund that is covered. So, they would be paying basically 12.5 percent of that fee. We don't think that onerous if in fact, and would be very willing to explore it further.

You are absolutely right. The last thing we want to do is disincentive this. We looked it as a way of ensuring that we would have enough money coming into that fund to cover any defaults in a conservative. This was all brought about the Credit Reform Act of 1990 requiring it.

It is not a user fee in that none of the fees go into the administration of the program. That money goes into a fund that would be there in case of default. We would be willing to make whatever adjustments, those that think hard about this, in order to get increased coverage by the amounts of money that we will have available.

We want to do it this year in order, again, to get some shipbuilding coverage and some significant modernization of some shipyards.

Mr. BATEMAN. Presently and in the administration's fiscal year 1996 program, the only thing in it that is positive or relates to commercial shipbuilding or stimulation of commercial shipbuilding is title XI. Would you comment on what's left and what happens when the OECD Agreement goes into force? Where are we then?

Admiral HERBERGER. If and when the OECD Agreement—

Mr. BATEMAN. I'm glad you said if and when.

Admiral HERBERGER. I'm probably going to regret saying that.

Mr. BATEMAN. It is music to my ears.

Admiral HERBERGER. My concern on the OECD is that after 5 years of negotiation, we have an agreement. I know there has been a lot of debate and a lot of criticism of the particular agreement.

My concern is that if we do not access the impact, if we stop the OECD Agreement and do not start down this process of trying to level the playing field in maybe the longer term rather than in the short term, will this country be in a position to give the kind of support that would match what the foreign governments had been and continue to give to their shipbuilding industry.

It would take a significant amount of government support to match what is out there today. So, the whole theme I thought behind the OECD was to begin the effort to level the playing field. I know there are flaws in it.

But before we totally stop the OECD Agreement, we had better understand fully what it would mean if the foreign countries continue to support their industries in competition to ours. That is my concern sitting where I sit. I am afraid that they will continue at a pace that has been almost overwhelming and we will not match it in timely fashion. Therefore, it will be very difficult for many of our yards to get back into some significant commercial shipbuilding.

Mr. BATEMAN. I'm sure, Admiral, you are conceptually aware of my concerns about the nature of the OECD Agreement. To state it very, very briefly, it isn't a matter of being opposed to an international agreement that levels the playing field.

The terms by which it is done and the timeframe within which it is done under this agreement may well leave us in a position where we don't have a team that can get on the playing field because our shipbuilding industry will have had its demise before that time.

I do have some very serious concerns about the specific nature of the agreement. Certainly, we want to have some testimony from the administration as it formulates its legislative proposals for the implementation of that agreement.

We will certainly want to explore the administration and our trade representatives going back and doing some renegotiating which I think is critical to our interest and which is supported by some very basic notions of equity and fairness.

I shouldn't be spending that much time making a statement as opposed to giving you all the opportunity to respond to the questions. Hopefully, that is helpful.

Mr. TAYLOR. Mr. Chairman, parliamentarily, did I yield to you or did you just take it back?

Mr. BATEMAN. I am not sure.

Mr. TAYLOR. I would like one brief question to followup on.

Mr. BATEMAN. I'm not sure which it is.

Mr. CUNNINGHAM. Parliamentary in question, Mr. Chairman.

You know, we sit here in between you and the minority leader. You have asked about 1½ hours of questions. I have asked 3 minutes of questions.

Mr. TAYLOR. You gave him 3 minutes.

Mr. BATEMAN. The Chair is going to plead guilty to having taken the time back and is now going to call on the gentleman from California who has been very patient.

Mr. CUNNINGHAM. First of all, I would like to set the record straight. There is only one person responsible for title XI money being put in, in the first Congress and he is sitting right here. He is Rusty.

You may remember your history, President Bush supported it. John Murtha supported it. Gerry Studds supported it. Our former chairman who is no longer with us supported it. But we had one stop and that was a guy named Dick Darmon. Mr. Darmon had stopped some other things which we all felt it would be good for Republicans and good for the President and good for jobs.

There was a caucus in which about 40 Members displayed a propensity to have Mr. Darmon not hold his position anymore while I took all 40 of those names and called Mr. Darmon and told him we were going to meet with a press conference if he continued to hold up title XI money.

We got it the very next day. Then Mr. Murtha came to me and said, well Duke, we know that you have been working on this hard, but you are a Republican and you are a minority. We can't let you take credit for it. So, we will tell you how good that you worked on it and what you did for it, but we got to take credit for the title XI funds.

Last year when the President signed it, he wouldn't even let me on the podium to talk about how things work. But I want to assure you that this panel has been fully bipartisan. As a matter of fact, the Merchant Marine Fisheries Committee that most of us served on was one of the most bipartisan committees that I have ever served on.

It was absolutely a pleasure to work on. I am sorry that it is disbanded. I wanted to make this panel a committee instead of just a panel. We do support title XI. When you talk about OPA-90 and you say foreign hauls, but at the same time we are sponsoring dual hauls so we don't end up with the pollution on our coasts.

We don't have a dozen Long Beaches along California. I think besides national security, that does help. It not only helps our jobs and the economy, it stimulates an industry that is chewing on bones to survive. I think everything that we can do, and I think Mr. Taylor stated it very well, we have absolutely got to support our shipbuilding, ship repair industry or it is going to die because foreign countries are subsidizing those things.

We in both Republican and Democratic administrations have not come out in strong support. We have got to change that. I am on the National Security Committee as well. I look at it not just from national security, but mostly from national security.

In looking at Desert Storm and the Russian hauls we had hauling our stuff, I know that Admiral Herberger, you talked about an

85-year-old gentleman and a 75-year-old gentleman that after Desert Storm marked down the front with Norman Schwarzkopf and Colin Powell because he was an 85-year-old man we had to bring back to tend those boilers and teach these kids how to sail these old ships.

Anything you can do to help us on this panel is—we are begging your help. I would say if you could comment briefly, Admiral, we talked about the ships tied up. A lot of folks are drawing money for those things tied up at the pier. Most of them are in the Reserve Fleet.

We talked about trying to get rid of those and what we can do maybe on this committee to get them overseas. They have got asbestos. It costs twice as much to refurbish them. Also, on the mark is the maritime academies. I think most of us support those. If we are going to increase the amount of maritime captains, then I would think that some of those academies are very important.

If both of you could just comment on the academies and how can we better have tied up that will never be used?

Admiral QUAST. Sir, first of all, let me say on the subject of the maritime academies, the Navy has just increased the number of graduates that we are taking from the maritime academies into the Navy, active duty reserve commissions which is what they all get.

We have historically looked to the academies as a source of high quality young officers that we are very appreciative of and require a whole lot less in the way of training dollars once they come on active duty because they have an education that aligns them to what we would like to use on our ships.

Surprisingly, a lot of them want to fly airplanes which is certainly not surprising to you, sir. We have and we support the continuation of the education that is at not only Kings Point, but the California Maritime Academy, where I taught myself. They put out a fine product. We would like to continue to see that product available to us.

As far as shipbuilding is concerned, one of the things, and Mr. Taylor was asking about RO/RO's and purchasing RO/RO's that are on the marketplace, I think one of the things that the Department of Defense should be recognized for is that we have a balanced program of meeting the requirements of that military requirement study.

A part of that balance is new construction. As a matter of fact, we are pumping close to \$6 billion into conversion and new construction of the large medium speed RO/RO ships that currently two yards, three yards are involved in.

Although not all of those are not appropriated for, if we reach the number of 19, which is spelled out in that mobility requirement study, that is about \$5.8 billion of ship construction or conversion, major repair conversion.

That is again a balanced approach; new construction for the long term, but purchasing what is available that we can get our hands on in the RO/RO for the short term because we are at 50 percent of the surge capacity.

Mr. CUNNINGHAM. Maybe I haven't followed along with our own legislation. It originally was 22. I know we allowed for foreign ships, 15 percent. Isn't that number supposed to be 22 for RO/RO's?

Admiral QUAUST. No, sir. The total number that is spelled out is 36 in the requirements. We are at 29 today. MARAD purchased two last month that will become available to us probably the next fiscal year after they get the updates to make them U.S. flagged. Then we still have a requirement for five that are outstanding.

In the 1996 budget, we are going to ask for enough money to buy hopefully three, but certainly two. That is about \$70 million.

Mr. BATEMAN. The gentleman from Maine, Mr. Longley, who has been very patient and has been here from the fall of the gavel.

Mr. LONGLEY. Thank you, Mr. Chairman.

Admiral, I wonder if you could provide any information on—apparently there is a proposal to shift the U.S. Merchant Marine Academy from the Department of Transportation to the Department of Defense.

Admiral HERBERGER. There is no official proposal.

Mr. LONGLEY. Is there any discussion on that?

Admiral HERBERGER. There has been. I have seen it in the media. I am not sure of the source. I would have to get back. I have seen it in print. But there is absolutely no initiative within the—

Mr. LONGLEY. If you could get some information on that.

Admiral HERBERGER. It is in Congressman Kasich's report. It is one line regarding shifting the Federal academy at Kings Point.

Mr. LONGLEY. If you have more information on that, plus I am curious as to whether there is anything pending that relates to the State maritime academies.

I appreciate your looking into that. Provide that for the record.

Admiral HERBERGER. Yes.

[The information referred to was not provided for the record.]

Mr. LONGLEY. I understand also that the Department of Defense recently completed a study in which it concluded that active commercial ships fitted with national defense features, I think such as refrigerated car carriers or that type of cargo ship, might offer a cost effective enhancement of military sealift capacity.

Would you agree that these types of vessels would enhance our Nation's military sealift capacity?

Admiral HERBERGER. Any addition of a military use of a vessel will enhance our capability. I think what we are facing now are the priorities of additional sealift. It is my understanding and Admiral Quast can back me on this, I hope, is that the first priority is to add the surge capability in the LMSR's, the 19 LMSR's, that are under conversion and/or construction, to add a significant capability.

That represents about at least 5 million square feet additional capacity. That coupled with the addition of the RRF RO/RO are the highest priorities that I am aware of coming out of this requirement for DOD.

I have not seen a specific requirement for a building charter or a program to support defense features on a new commercial ship. I think it is a matter of what the priorities are today, what will come first with the resources that will be available.

Mr. LONGLEY. The study apparently concluded that these ships could be available for defense operations at time intervals of anywhere from 1 to 11 days. I am wondering how that would compare with the scheduled breakups of the laid up Ready Reserve Force?

Admiral HERBERGER. The RO/RO capacity of both the, obviously the prepositioned force that are out on station and can move towards an area rather quickly; and then those that will be back in the United States or outport at other places will be on a 96-hour tether, probably just like they are today, similar to our fast sealift ships. So, very responsive.

The vessels in the RRF, the RO/RO, the 22 we have today going toward 29, they are kept in a 4-day standby with a 10-man nucleus crew ready to light off.

The first example we had of how effective that was, was for the Haitian operation where we were able to get out all 14 vessels called for in less than the 4 days. The fleet of RO/RO ships that we have today and that we envision for the future will be very responsive.

Mr. LONGLEY. Let me just follow up, and Admiral, I would like to get your response too, to these questions. To what extent are there some advantages in increasing the number of active ships that might be available in time of need versus not only the cost of maintaining the Ready Reserve Fleet, but to what extent are there disadvantages of taking ships that have been tied up for some period of time and attempting to make them seaworthy and bringing them to use on a relatively quick basis?

Admiral HERBERGER. If there was enough funding, enough support, an active fleet, in my mind, is very beneficial. A ship that is out there active with a crew operating day in and day out is an extremely good asset to have for sealift.

What we have learned from Desert Storm and Desert Shield is that if we want the vessels in the RRF to be ready on the schedule that they need them, we need to put more resources in them. What we are having now is an effort to fill that intermediate goal of increasing today's requirement.

In the long term we obviously have to look and see are we going to continue to maintain used ships in the RRF or would an active fleet, fully operational, be better. I would prefer to see an active fleet, fully operational. That, today, would be a very expensive walkup.

Mr. LONGLEY. Admiral Quast, any thoughts on those questions?

Admiral QUAST. Yes, sir. I think the study that you are referring to is the national defense features study that was just promulgated by the Department of Defense earlier this month. It was viewed as a viable alternative to replacing some of the old RRF ships that we have currently in the RRF, some of the bulk ships that toward the end of the century, we will have to make some decisions as to what we are going to do.

Are we going to replace RRF ships? Why are we going to find another option or another alternative? The Department of Defense uses as an alternative to replacing at the end of the century these bulk ships that are currently in the RRF, a viable alternative.

Again, Admiral Herberger mentioned the fact that funds for this national defense features program have to be determined. There are certainly no funds in the program as we know. I am not certain, but I would be very doubtful that the Department of Defense under the current program would sponsor it.

Certainly there is nothing in the program for that. I believe that is what you are referring to. It has some appeal. They are active ships used in a commercial marketplace with crews. They are kept up maintenance wise. They are in operational condition.

If they could be made available to us in a relatively short period of time, the days that you mentioned, up to 10 days, that certainly would be a very viable alternative. It is not, from the Department of Defense's view, not to interrupt or in any way deter what we have as a goal. The RO/RO is in the LMSR's and the national sea-lift fund.

Mr. LONGLEY. Mr. Chairman, if I could ask one more question.

Mr. BATEMAN. Yes.

Mr. LONGLEY. Admiral Herberger, you made reference to a study of the potential need for mariners. I am wondering if you are referring to any particular study and/or does that information also include figures on the maritime or the shipbuilding industrial base, particularly the number of jobs at stake and the extent to which those shipbuilding jobs might be jeopardized if our current policies continue?

Admiral HERBERGER. I will provide the specifics. It was an international maritime organization sponsored study. I don't have the title readily available.

Mr. LONGLEY. We would appreciate that for the record.

Admiral HERBERGER. I definitely will. The subject was mariners and the need to improve the quality and to ensure that we had a supply of well educated well trained. I don't believe there was another section regarding shipbuilding. I don't want to mix the two subjects.

[The information referred to follows:]



U.S. Department
of Transportation

Maritime
Administration

Washington, DC 20590

**Outlook
for the
U.S. Shipbuilding
and
Repair Industry
- 1995 -**

1995 OUTLOOK FOR U.S. SHIPBUILDING AND REPAIR

Overview

The United States shipbuilding industry is going through a time of dynamic change. Since the enactment of the National Shipbuilding and Shipyard Conversion Act of 1993, U.S. shipyards have been aggressively competing for re-entry into the domestic and foreign commercial shipbuilding markets. The newly expanded Title XI financing guarantee program has been a major impetus to the shipyards fostering this renewed competition. During 1994, seven companies received approval for Title XI loan guarantees to construct a total of 52 ships and barges in U.S. shipyards. This includes the first order for U.S.-built ocean going commercial ships for export since 1957. Title XI financial guarantees were also extended and approved for two shipyard capital improvement and modernization projects. The severe contraction in Navy work has forced U.S. shipyards to search harder for commercial work in order to survive. The Navy's proposed fiscal year (FY) 1995-1999 shipbuilding program will average less than eight new ships per year, compared with an average of nineteen new ships annually in the 1980's. As industry and the government focus their efforts towards revitalization, the downturn in naval construction activity will continue to be the most important challenge for the major U.S. shipbuilders during the rest of this decade. The second-tier shipyards, with small or medium size facilities, are currently building a variety of vessels for use on the inland and coastal waterways. The prospects for these shipyards continue to be bright for the remainder of the 1990's.

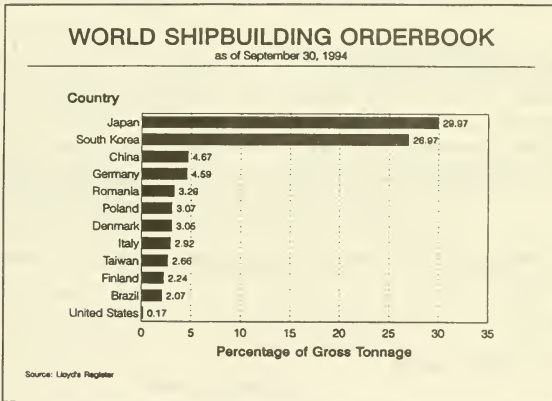
World Market

The number of ships on order or under construction for the world market increased slightly in 1994 from the previous year. As of October 1994, the world orderbook

for merchant vessels, 100 gross tons (gt) and over, consisted of 2,098 vessels totaling 42.0 million gt. This reflects a 4.1 percent decrease from the 2,188 vessels on order a year earlier, and more significantly a 11.1 percent increase in gross tonnage from 37.9 million gt. The average size of merchant ships on order increased by nearly 16 percent from 17,313 gt to 20,055 gt.

Japan continues to lead the world in merchant shipbuilding. As of October 1994, it commanded 30.0 percent of the gross tonnage of merchant ships on order, followed by South Korea with 27.0 percent and the People's Republic of China a distant third with 4.7 percent (Chart 1). The United States was 26th, with only 0.2 percent of the world gross tonnage.

Chart 1



U.S. Shipbuilding

In past years the benchmark used for tracking the U.S. shipbuilding industry was the Active Shipbuilding Base (ASB), which was defined by shipyard capability and business criteria. Because of the significant reduction in new ship construction, especially 1,000 gross tons and over, the ASB has been replaced by a base defined primarily by shipyard capability. This new shipyard base is called the U.S. Major Shipbuilding Base (MSB) and is defined as privately owned shipyards that are open, having at least one shipbuilding position, consisting of an inclined way, a launching platform, or a building basin capable of accommodating a vessel 122 meters in length or over. With few exceptions, these shipbuilding facilities are also major repair facilities with drydocking capability. Utilizing this definition, as of January 1, 1995, there were 21 major shipbuilding facilities in the United States.

According to the Department of Labor, aggregate employment involved in shipbuilding and repair was 108,000 in mid-1994, down only 1,000 from the previous year. The MSB shipyards employ about 71 percent of the total work force of the shipbuilding and ship repair industry. The remaining 29 percent was in the 550 additional establishments (with 10 or more employees) classified under Bureau of Labor Statistics SIC 3731 (Shipbuilding and Repairing). Not included in SIC 3731 are the nine Government-owned shipyards, which do not engage in new construction, but rather overhaul and repair Navy and Coast Guard ships. As of October 1994, the total employment in the nine Government-owned shipyards was 45,700.

Federal Assistance Programs

The Maritime Administration (MARAD) provides financial assistance to U.S. shipowners through the Federal Ship Financing Program (Title XI) and the Capital Construction Fund (CCF) program.

The Title XI program was established by the Merchant Marine Act of 1936, as amended, and provides for a full faith and credit guarantee by the United States Government for the purpose of promoting the growth and modernization of the U.S. merchant marine and U.S. shipyards. Prior to November 30, 1993, the Title XI program provided for Federal Government guarantees of private sector financing or refinancing obligations for the construction or reconstruction of U.S. flag vessels in U.S. shipyards. Vessels eligible for Title XI assistance include commercial vessels such as passenger, bulkers, cargo, tankers, tugs, towboats, barges, dredges, oceanographic research, pollution abatement, offshore oil vessels and floating drydocks.

On November 30, 1993, Congress passed the National Defense Authorization Act for FY 1994, which contained a section subtitled "National Shipbuilding and Shipyard Conversion Act of 1993." This Act provided the Secretary of Transportation with the authority to extend Title XI guarantees for eligible vessels constructed, reconstructed or reconditioned in a U.S. shipyard and for shipyard modernization and improvement.

MARAD also permits U.S. operators to establish a Capital Construction Fund. The operator can use tax-deferred dollars in the Fund for qualified withdrawals to procure new or reconstructed vessels from U.S. shipyards.

In October 1993, the Clinton Administration issued a report *Strengthening America's Shipyards: A Plan for Competing in the International Market*, which outlines actions to assist the struggling U.S. shipbuilding industry. The President's five point plan includes:

- Ensuring fair international competition
- Eliminating unnecessary government regulation
- Assisting international marketing
- Financing ship sales through Title XI loan guarantees
- Improving commercial competitiveness with MARITECH

The MARITECH program is a jointly funded Government/industry effort administered through the Department of Defense's Advanced Research Projects Agency (ARPA), in consultation with MARAD. The program's main thrust is to develop and apply advanced technology to improve the international commercial competitiveness of the U.S. shipbuilding industry. In addition, MARITECH is being executed in full partnership with the Navy, through the Office of Naval Research. The MARITECH program has a proposed five year life span during which time it could invest as much as \$220 million in Federal money into shipbuilding and related production technology. MARITECH awards matching federal funds, up to 50 percent, on a competitive basis, to develop and implement technologies and advanced processes for the competitive design, marketing, production, and support of commercial ships, resulting in a total infusion of up to \$440 million into related research and development. MARITECH was funded at \$30 million in FY 1994 and at \$40 million in FY 1995. MARITECH is a significant complement to the President's Defense Reinvestment and Conversion Initiative to preserve the critical shipbuilding industrial base which is vital to our country's national security.

MARITECH is an industry led, industry driven program which manages cooperative projects between the public and private sectors that will assist U.S. shipyards in competing more effectively in the international market. MARITECH's focus is divided into two parts, near-term market penetration and longer-term advanced technology development, implementation and achieving an infrastructure for ongoing technical innovation. In addition, MARITECH focuses on the development of innovative ship and ship systems technologies resulting in customer-oriented commercial ship products for domestic and export sale, coupled with the development and integration of shipbuilding technologies to enhance U.S. shipyard productivity.

Thirty-four proposals were submitted for consideration and twenty were selected to receive government funding for FY 1994. Projects submitted included a broad selection of ship types: double hull tankers, passenger vessels, dry and bulk cargo

ships, container vessels, high-speed ferries and offshore service craft. Selected projects are summarized in Table 1:

Table 1

Summary of Proposals Selected for MARITECH Funding		
Project	Lead Contractor	FY 94 Government Funding
Vessel Design Projects		
40,000 dwt Double Hull Product Carrier 85,000 dwt Double Hull OBO Carrier	Alabama Shipyard	\$ 3,000,000
125,000 dwt Double Hull Tanker 324,000 dwt Double Hull Tanker	Merinex International	\$ 1,800,000
Medium-sized Multipurpose Ship	Halter Marine	\$ 400,000
23,000 dwt Container/Bulk Carrier	Halter Marine	\$ 1,000,000
Small Vessel Design and International Market Analysis	American Waterways Shipyard Conference	\$ 600,000
High Speed Mono Hull Focused Technology	Bath Iron Works	\$ 600,000
Cruise Ship Preliminary Design Manufacturing Plan, and Market Analysis	Ingalls Shipbuilding	\$ 1,100,000
Car Carrier Design, Build Strategy, Marketing and Finance Plans	National Steel Shipbuilding	\$ 200,000
Shipyard/Technology Projects		
See Horse Self-Elevating Offshore Support Platforms	Bollinger Machine Shop and Shipyard	\$ 1,500,000
Commercialization of Planning SWATH Technology	Halter Marine	\$ 300,000
Shipyard Conversion for Construction of a 40,000 dwt Tanker	Newport News Shipbuilding	\$ 3,000,000
Design of a Virtual Shipyard	U.S. Shipbuilding Consortium	\$ 1,600,000
Modern Manufacturing Methods and Information Systems	Todd Pacific Shipyards	\$ 1,600,000

The Federal Government also provides significant direct support to the industry through the purchase and repair of ships, and the procurement of goods and services from a large number of shipyards and related industries. Principal

contracting Government agencies include the Naval Sea Systems Command, the Military Sealift Command, the Army Corps of Engineers, the U.S. Coast Guard, the National Oceanic and Atmospheric Administration, the National Science Foundation, and the Maritime Administration.

The value of work completed by U.S. shipyards in 1994 totaled \$9.4 billion, down nearly 4 percent in constant dollars from 1993. The continuing depressed state of the commercial shipbuilding industry in the United States and the winding down of military procurement have caused some U.S. shipyards to close or enter into bankruptcy proceedings during the past few years.

Commercial Ship Construction

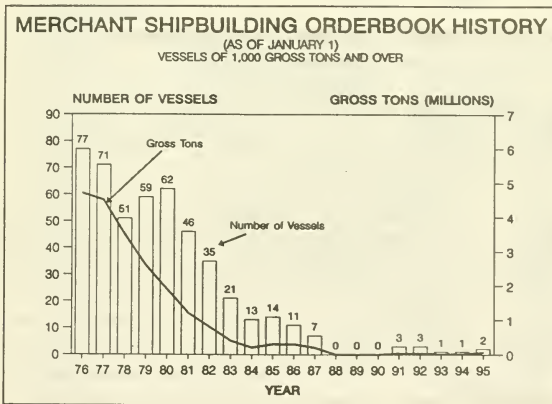
In 1994, the U.S. shipbuilding industry received its first ocean going commercial ship order since 1990. This order also represented the first ships ordered by a foreign ship owner in more than 35 years.

On October 31, 1994, Newport News Shipbuilding signed a contract to build two 46,500 dwt, "Double Eagle," double hulled petroleum tankers with Eletson Corporation, a Greek shipping company, with an option for two more tankers. This contract represented Newport News' return to the commercial shipbuilding market. This is the first commercial ship order from a foreign buyer to a U.S. shipyard since 1957 and these will be the first commercial ships built by Newport News since it delivered two supertankers to Shell Oil in 1979. MARAD provided \$133.5 million in financing guarantees under the recently expanded Title XI program for Eletson Corporation to procure these vessels; the contract is worth approximately \$153 million. The Double Eagle tankers will be built using modern shipbuilding techniques that involve manufacturing ships in a series, in order to minimize design and engineering costs and to facilitate the standardization of parts.

On December 19, 1994, BethShip's Sparrows Point Yard received an order from Hale Intermodal Transport Co., for the construction of four 79-meter oceangoing barges capable of holding 450 TEU containers. This is an \$8 million order for BethShip's Sparrows Point Yard and will be the first vessels built at the yard since 1988. The barges will be classified by the American Bureau of Shipping (ABS) and will be capable of sailing worldwide. Construction of the first barge, the *Providence Trader*, will take about seven months.

As of January 1, 1995, the U.S. orderbook for commercial shipbuilding consisted of the two 46,500 dwt, "Double Eagle," double hulled petroleum tankers with Eletson Corporation at Newport News and the four 79-meter oceangoing non-self-propelled barges at BethShip's Sparrows Point Yard. It should be noted that another vessel, the *American Queen*, a 3,950 gross ton paddlewheel boat being built by McDermott, is not oceangoing. The self-propelled ship orderbook since 1976 is illustrated in Chart 2.

Chart 2



Military Ship Construction

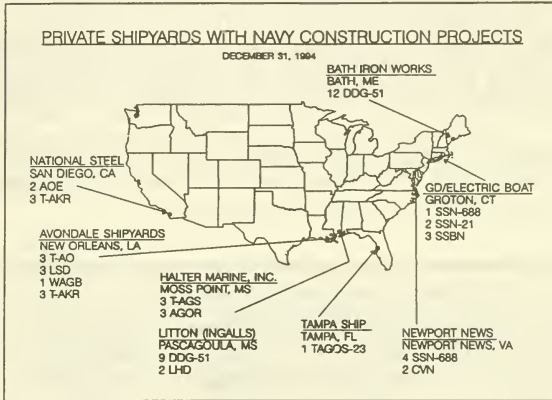
During the 1980's, the U.S. Navy commenced the largest combatant ship construction program in peacetime history, with Congress appropriating nearly \$100 billion. Since 1991, Navy construction programs have been on the decline and are projected to continue to diminish throughout the remainder of the 1990's. 1994 witnessed the Navy's continuing domination of the workload in U.S. shipyards. During 1994, the Navy ordered 11 new vessels of 1,000 light displacement tons (ldt) or larger from U.S. private shipyards, while 15 new Navy vessels were delivered. As of December 31, 1994, Navy vessels of 1,000 ldt or larger on order or under construction totaled 57 ships, of which 18 are scheduled to be delivered by the end of 1995 (Table 2). An additional 18 LCACs, PCs, MHCs and TAKR(C)s are also scheduled to be delivered before the end of 1995. However, as a consequence of the austere Navy new construction budget, the Navy's program will continue to be sharply diminished during the remainder of this decade.

Table 2

Military Ships Under Construction (1,000 ldt or Greater) December 31, 1994		
Symbol	Type	Number
AOE	Fast Combat Support Ship	2
CVN	Aircraft Carrier (Nuclear-powered)	2
DDG	Guided Missile Destroyer	21
LHD	Amphibious Assault Ship (Multi-purpose)	2
LSD	Dock Landing Ship	3
SSN-21	Attack Submarine (Nuclear-powered)	2
SSN-688	Attack Submarine (Nuclear-powered)	5
SSBN	Ballistic Missile Submarine (Nuclear-powered)	3
AGOR	Oceanographic Research Ship	3
TAKR	Strategic Sealift	6
WAGB	Ice Breaker	1
T-AGOS-23	Ocean Surveillance Ship	1
T-AGS-60	Ocean Survey Ship	3
T-AO	Fleet Oiler	3
Total Military Ships		57

Eight privately owned shipyards had contracts for the construction of naval vessels. The naval shipbuilding orderbook includes a variety of vessels from ballistic missile submarines to fleet oilers and a Coast Guard icebreaker. The Navy's new construction backlog of 57 ships is comprised of 14 different types, and the orders are dispersed among 8 private shipyards located on the Atlantic (3), the Gulf (4) and Pacific (1) coasts (Chart 3).

Chart 3



Most U.S. shipyards do not have the experience or expertise required to construct sophisticated naval combatant vessels. The Navy's T-ship projects, however, are providing some work for four private U.S. shipyards (Tampa Ship, Halter Marine - Moss Point, Avondale Shipyards and National Steel and Shipbuilding Co.) that have for the last decade relied on military ship construction. These projects are for the building of civilian-manned Navy auxiliary ships under control of the Military Sealift Command (MSC).

On September 2, 1993, MSC announced the award of the first contract for a strategic sealift ship detail design and construction to Avondale Industries, Inc., of New Orleans, LA. The contract was for one ship priced at \$265.2 million. Since then Avondale Industries, Inc., has received contracts for two additional strategic sealift ships, and still holds the options for three more ships, for a total value of \$1.3 billion. Contract completion is scheduled for April 30, 2001. On September 15, 1993, MSC announced the award of a contract for the second strategic sealift ship detail design and construction to National Steel and Shipbuilding Co. (NASSCO) of San Diego, CA. The contract was priced at \$269.1 million. NASSCO has since received contracts for two additional strategic sealift ships and is also holding the option for three more ships, for a total contract value of \$1.3 billion. The contract is scheduled for completion by April 30, 2001.

As of December 31, 1994, there were 13 T-ships on order or under construction, up from 10 one year ago. The increase in the number of T-ships on order is due to the recent awards for the six strategic sealift ships (Table 3).

Table 3

T-SHIPS ON ORDER OR UNDER CONSTRUCTION (as of December 31, 1994)			
Shipyard	Ship Identifier	Vessel Name	Estimated Delivery Date
Tampa	T-AGOS 23	IMPECCABLE	01/31/95
Halter Marine	T-AGS 61	SUMNER	05/01/95
Avondale	T-AO 201	PATUXENT	06/07/95
Avondale	T-AO 204	RAPPAHANNOCK	11/07/95
Halter Marine	T-AGS 62	BOWDITCH	11/29/95
Avondale	T-AO 203	LARAMIE	04/05/96
Avondale	T-AKR 300	BOB HOPE	08/30/97
National Steel	T-AKR 310	- unnamed -	09/30/97
Halter Marine	T-AGS 63	- unnamed -	01/30/98
Avondale	T-AKR 301	- unnamed -	04/30/98
National Steel	T-AKR 311	- unnamed -	04/30/98
Avondale	T-AKR 302	- unnamed -	10/30/98
National Steel	T-AKR 312	- unnamed -	01/30/99
TOTAL	13 Ships		

National Oceanic and Atmospheric Administration

The National Oceanic and Atmospheric Administration's (NOAA) Fleet Replacement and Modernization (FRAM) Program was begun in FY 1992. The program continues in FY 1995 with routine and critical maintenance of the existing fleet, the construction of an oceanographic research ship (AGOR) at Halter Marine, Inc. Moss Point, LA, the conversion of a T-AGOS vessel to a NOAA oceanographic vessel, a repair to extend (RTE) of the fisheries research vessel *Delaware II*, and a solicitation for design concepts with an option for the construction or lease of a low endurance fisheries research vessel. The conversion and RTE are currently in source selection and the solicitation for the low endurance fisheries research vessel has been issued. Design and specification development also continues for the RTE of another existing fisheries research vessel, the *Miller Freeman*, and the conversion of a T-AGOS to support the Alaskan mapping and charting mission as well as other ships.

Ship Repair

The U.S. ship repair industry continues to be very active, and U.S. shipyards are competing aggressively in the domestic and foreign markets for ship repair and conversion work as a replacement for diminishing Navy orders.

The U.S. Navy's primary resources for ship repair are 36 privately owned shipyards and 8 naval shipyards. U.S. shipyards, both large and small, are turning to commercial ship repair work because of the continuing decline in the Navy's new shipbuilding activities and a delay in hoped-for commercial shipbuilding orders.

U.S. shipyards benefit from their location in the United States (the world's most important trading nation) because of the large volume of goods transiting U.S. ports. Therefore, location, timeliness of repairs, and competitive prices can give U.S. shipyards an edge over many foreign repair yards.

Marine Hydraulics International, Inc., Norfolk, VA, was awarded a \$10 million contract in July 1993 by MARAD to convert the tanker *Mt Washington* to an Offshore Petroleum Discharge System (OPDS) ship. This vessel can discharge fuels for military vehicles and aircraft through up to almost seven kilometers of flexible discharge lines while anchored offshore. This is the fifth in a series of tankers converted into OPDS ships for the U.S. Government.

Eastern Technical Enterprises, Inc., Brooklyn, NY, was awarded a \$9.5 million contract in February 1994 by MARAD to convert, reactivate, and repair the *USNS Harkness* at its production facility located in the former Brooklyn Navy Yard. This vessel was a naval survey ship and will be used as a Public Nautical Schoolship for the Maine Maritime Academy. The contract work is scheduled for completion in April 1995.

Stevens Technical Services, Inc., Brooklyn, NY, was awarded a \$7.8 million contract in June 1994 by MARAD to convert, reactivate, and repair the *USNS Chauvenet*. This vessel was also a naval survey ship and will be used as a Public Nautical Schoolship for the Texas State Maritime Academy. The contract work is scheduled for completion in June 1995.

These ships will meet all applicable U.S. Coast Guard, ABS, and MARAD requirements, including a two compartment standard for subdivision and fireproof construction. Once converted, the schoolships will be used by the respective maritime academies to train deck and engine officers for the U.S. merchant marine.

The FY 1995 budget request for Navy ship repair and fleet modernization is \$3.2 billion, an increase of about 15 percent from the FY 1994 appropriation. The budget request is almost 8.5 percent lower than the FY 1993 appropriation, and 31 percent below the FY 1990 appropriation.

Each year the Navy accomplishes maintenance and modernization work on its ships through both the public and private shipyards. In FY 1994, the Navy completed

146 availabilities (overhaul/repair work) with a budgeted value of approximately \$2.8 billion. Of these, 54 were accomplished in the public sector's Naval shipyards for a total budgeted value of \$1.9 billion (67 percent) while the private sector completed 92 smaller, less complex availabilities generating approximately \$931 million (33 percent) in budgeted value. The FY 1995 projected split is \$1.9 billion (59 percent) in the public sector and \$1.3 billion (41 percent) in the private sector of the Navy's maintenance FY 1995 budgeted total of \$3.2 billion. At present, the public/private competition is being held in abeyance for FY 1995.

Before 1985, Navy repair work was either allocated directly to public yards or awarded to private yards. The majority of ship repair work is still distributed on an allocation basis. However, in FY 1985, the Navy launched its ship repair competition test program between public and private shipyards. Under competitive bidding, most submarine repairs have gone to the public shipyards, while the private sector has won the bulk of the contracts for surface ship repairs.

In 1990, the Congress established a new set of procedures for military base closures (Title XXIX of P.L. 101-510). These procedures are valid for five years with closures being proposed every other year -- 1991, 1993, and 1995. The closure of Navy shipyard facilities during the next few years, as a result of recommendations by the Base Closure and Realignment Commission appointed by the President, could have an impact on both public and private shipyards. As of October 1, 1993, the Commission has recommended the closure of Philadelphia Naval Shipyard, Philadelphia, PA, Mare Island Naval Shipyard, Vallejo, CA, and Charleston Naval Shipyard, Charleston, SC.

MARAD's National Defense Reserve Fleet (NDRF) provides a steady source of ship repair work. As of January 1, 1995, the fleet consisted of 215 merchant vessels and 74 military vessels. Many of these vessels can be activated to meet the shipping requirements of the United States in the event of a national emergency.

A key element of the NDRF is the Ready Reserve Force (RRF), which as of October 1, 1994, was composed of 89 vessels. The number of vessels in the RRF reached as high as 102 during FY 1994, but the recent downgrading of ten breakbulk vessels and six tankers has substantially reduced the number of vessels to be maintained. This downgrading was necessary since the Congress appropriated approximately \$100 million less than the President's FY 1995 request for NDRF maintenance and operations.

For FY 1995 MARAD estimates that an average of \$1.2 million per vessel will be spent for the maintenance, berthing, and crewing of RRF vessels, of which approximately \$700,000 will be spent directly on maintenance and repair. For FY 1996, the maintenance and repair expenditure will increase to \$1.6 million per vessel if implementation of the Department of Defense's (DOD's) Mobilization Requirements Study is fully funded.

Although the RRF was projected to expand to 140 ships by the end of FY 1999, it appears that the future size of the RRF will remain at or below 100 ships. It is planned that two additional RO/RO's will be purchased for the RRF during FY 1995. The upgrade work for these two vessels will be performed in U.S. shipyards. Past upgrades of this type averaged \$10 million per vessel.

MARAD upgraded eight ships in several East Coast shipyards for use by the U.S. Army as sealift assets, pre-positioned at strategic locations overseas. The eight ships, comprised of seven roll on/roll off (RO/RO) ships and one auxiliary crane ship, were selected from the RRF fleet to meet the Army's requirements to deploy a divisional unit of equipment, supplies, and ammunition to a remote theater of operation in a short time. The first ship arrived at its pre-positioning site on January 19, 1994, with the final ship arriving July 3, 1994. It is envisioned that these vessels will remain as part of the pre-positioned fleet until mid-1997, at which time they will be returned to MARAD.

Passenger and Cruise Vessels

In 1994, U.S. shipyards were not involved with any major construction or conversion projects of oceangoing passenger and cruise ships. The shipyards were, however, involved with several significant repair projects.

Avondale Industries, New Orleans, LA, performed some emergency repairs on Holland America Line's 1,214 passenger, 199 meter *Noordam*, after it was involved in a collision with a Greek cargo ship in the Gulf of Mexico. During a ten-day drydocking, Avondale repaired a 26 meter x 18 meter hole in the aft starboard side of the ship and performed some interior repairs.

Southwest Marine, San Diego, CA, redelivered the Princess Cruise Line's TSS *Fair Princess* after some routine drydocking and maintenance that included underwater hull and topside painting, as well as work on the main engines, shafting and generators.

Newport News Shipbuilding, Newport News, VA, drydocked the world's largest cruise liner, the *Norway*, for its owner, Kloster. Newport News Shipbuilding and NORSHIPCO, Norfolk, VA, cooperated in the repair and drydocking of ten Sea-Land containerships, which were completed in four weeks. Newport News Shipbuilding also won a contract for the renovation of the U.S.-flag cruise liner *Independence*.

A myriad of U.S. shipyards continue to be involved in the design and construction of passenger, cruise, dining and gaming vessels. These projects have been generated by the enactment of state legislation permitting riverboat gambling and the Flower Banks National Marine Sanctuary Act (Public Law 102-251), which allows gambling and gaming devices on board U.S. flag ships on "cruises to nowhere." Riverboat gambling is reportedly now legal in six states and is under consideration in 15 more states. Riverboat gaming was approved this past November in the states of Missouri and Indiana. This legislation has spurred the rise in riverboat gambling with new boats appearing, especially in the Mississippi

River basin and the Gulf Coast area. The passage of riverboat gaming in both Missouri and Indiana could provide a market for up to 18 new gaming vessels.

The riverboat gaming industry is less than three years old and has been a boon to both shipyards and suppliers with a customer demand creating backlogs of 18 to 24 months in some yards. Some sources predict market expansion will continue to 80 or 90 boats on the Mississippi River alone with casino revenues expected to reach \$3 billion within two years. Some of the recent deliveries are listed in Table 4:

Table 4

RECENT DELIVERIES OF SMALLER PASSENGER AND CRUISE VESSELS

VESSEL NAME	VESSEL TYPE	BUILT BY	LENGTH x BEAM (m)
Argosy IV	Sidewheel Casino	Alabama Shipyard	73 x 23
Belle of Baton Rouge	Paddlewheel/Gaming	Avondale Industries	81 x 23
Casino Queen	Passenger/Gaming	Patti Shipyard, Inc.	136 x 21
Emerald Clipper	Dinner	Washburn & Doughty	46 x 10
Friendship IV	Whale Watching Excursion	Gladding-Hearn	28 x 9
Grand Victoria	Casino	Watch City Shipyard	122 x 34
Kenai Explorer II	Tour	Westport Shipyard, Inc.	27 x 7
Kona Aggressor II	Dive	Nichols Brothers Boat Bldrs	24 x 9
Island Girl VI	Dinner Excursion	Skipper Liner Ind., Inc.	24 x 6
Martha's Vineyard	Car/Passenger Ferry	Atlantic Marine, Inc.	70 x 18
Mexico III	Ferry	Breaux Bay Craft	46 x 9
Miss New York	Excursion	Blount Industries, Inc.	40 x 10
Odyssey II	Passenger/Dinner	Service Marine Ind., Inc.	61 x 12
Players Riverboat Casino II	Casino	Leevac Shipyards	73 x 16
Royal Queen	Dinner Cruise	Service Marine Ind., Inc.	31 x 8
Star Casino	Gaming	Bender Shipbuilding	76 x 24

Although the demand for casino boats is still high, interest in the other types of boats is also starting to grow. It is reported that there is a healthy market for passenger boats that are not casino boats, with the steady growth in the excursion and dinner cruise markets. Another, non-gaming boat sector of the passenger boat market that looks to be in for some growth is ferries. In 1994, contracts were awarded for the construction of new ferries for the states of North Carolina,

Virginia and Texas. Virginia has an option for two additional ferries which would bring the contract value to over \$33 million.

Second-Tier Shipyards

The small-size and medium-size shipyards, often referred to as "second-tier shipyards," comprise another important sector of the U.S. shipbuilding and ship repair industry. These shipyards are primarily engaged in supporting inland waterway and coastal carriers. Their market is the construction and repair of smaller type vessels, such as tug boats, supply boats, ferries, fishing vessels, barges, and small military and Government-owned vessels. During 1994 these second-tier shipyards delivered or commenced the construction of about 649 powered vessels and 943 barges, a significant increase over the previous year. In addition, passenger vessels registered a 22 percent increase, largely due to the increase in the demand for gaming boats.

The second-tier yards are fiercely competitive and innovative. Some of the second-tier shipyards are competitive in the international marketplace and have successfully built vessels for export. Some examples of recent awards and buildings for the export market include:

A 43-meter triple-screw, 4,500 horsepower towboat and 12 hopper barges to be built by Trinity Marine Group, New Orleans, LA, for use in transporting grain on waterways throughout Paraguay, Brazil, Argentina, Bolivia and Uruguay.

AMFELS, Brownsville, TX, is building two drill barges for employment in Lake Maracaibo, Venezuela.

Eleven 24-meter fast patrol boats for the Philippine Navy will be built by Trinity Marine Group's Equitable Shipyard in New Orleans, LA. This order is worth \$27.5 million.

The first of two 35-meter patrol boats being built by Bender Shipbuilding, Mobile, AL, was delivered for the Colombian Navy.

In the late 1970's and the early 1980's, expectations of increased demand for barges that would carry grain and coal to coastal ports for export markets led to a construction boom in the second-tier shipyards. When strong demand failed to emerge, surplus capacity developed and the shipyards turned to building to satisfy the increased demand for small military vessels. As government contracts dry up, second-tier shipyards are looking for other areas to absorb the industry's excess capacity. One specific area is overseas. Second-tier shipyards are looking for ways that will allow them to participate in international markets for the construction of small ships. These shipyards believe that they must expand internationally in order to survive.

New Construction activity, as reported by the American Waterways Shipyard Conference (AWSC) in their 1993 Annual Shipyard Survey, shows, compared to the previous year, an increase of approximately 26 percent in power driven vessels, from 117 to 147, a 12 percent decrease in river barges, from 765 to 675, and an increase in the overall construction of new offshore barges of 712.5 percent with the construction of offshore tank barges increasing 100 percent.

It is reported that during 1994 that the power driven vessels posted the largest gains with pushboats, towboats and tugs increasing 114 percent over 1993 numbers. Other sectors also posted increases: crewboats and personnel boats, 45 percent; passenger vessels, 22 percent; and military vessels 20 percent. Decreases were seen in other parts of the industry, with the construction of spill recovery/response boats decreasing 45 percent and research/survey hull decreasing 50 percent.

A few examples of new construction activities in the second-tier shipyards are:

One barge launched during 1993 was a 65,000 barrel tank barge built by Zidell Marine Corp., Portland, OR. The barge, 83 meters x 27 meters x 6 meters, is the largest double-hulled tank barge operating on the inland waterway system.

Trinity Marine, Madisonville, LA, delivered the first of 16 super-jumbo hopper barges to Mid-South Towing Company. The 79 meter x 16 meter barges can carry twice the cargo, about 3,350 tons, at the same operating draft of 2.9 meters.

\$20 million worth of equipment for the Nigerian offshore oil industry was built by three Louisiana boatyards. Equipment consisted of towboats, deck barges, fuel barges, self-propelled tank barges, drydock, and spare parts.

The approval for riverboat casino gambling by a number of states has created a building boom for smaller shipyards. If each state considering the issue approves gambling, this important new market should be around for some time. The revived and expanded Federal Ship Financing Program (Title XI) has already had some favorable impact on the work available in the second-tier shipyards.

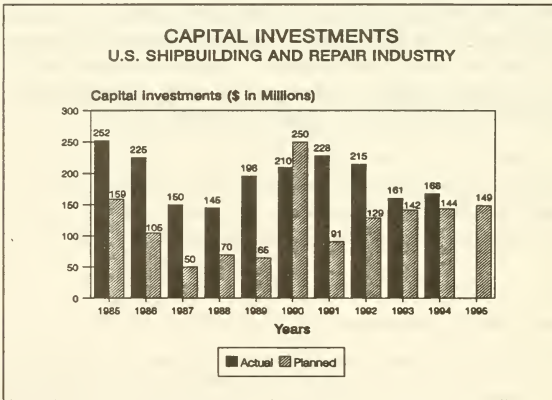
Second-tier shipyard repair activities overall declined in 1993 over 1992 for the second straight year. The survey showed a 13 percent increase in the number of power driven vessels repaired, from 5,827 to 6,571. The repair of fishing vessels increased 49 percent, and repair of ferries and passenger vessels increased 72 percent, from 137 to 236. Repair to river barges decreased 11.5 percent with repairs to deck barges decreasing 45 percent. Repairs to river tank barges decreased 36 percent. Repairs to offshore barges also decreased between 1992 and 1993 slightly more than 20 percent, from 508 to 404.

Capital Investment

During FY 1994, the U.S. shipbuilding and repair industry invested an estimated \$168 million in the upgrading and expansion of facilities. Much of this investment went to improve the efficiency and competitiveness of the shipyards. In 1995, the industry is forecast to spend \$149 million, according to data received by MARAD. The industry's estimated capital investments since 1970 have totaled \$5.4 billion, and actual expenditures since 1985 have consistently exceeded those planned, except in 1990 (Chart 4).

Capital investments have included building basins, floating drydocks, cranes, automated equipment, and highly mechanized production systems. Emphasis has been put on introducing modular techniques--the fabrication of large sub-assemblies and pre-outfitting of ship components.

Chart 4



Outlook for 1995

U.S. shipyards are expanding their penetration into the commercial shipbuilding market. The order for the construction of two product tankers for export and the healthy backlog of proposed commercial shipbuilding projects forecasts the probable expansion of the U.S. shipbuilding orderbook. For the foreseeable future, the U.S. shipbuilding and repair industry will continue to be dominated by Navy shipbuilding, conversion and repair work, although at a significantly lower level of activity than was experienced during the past decade. The Navy shipbuilding budget has been declining for a number of years. As the result of the authorization for a new aircraft carrier, the FY 1995 Navy budget is \$5.6 billion, 32 percent higher than what was appropriated in FY 1994. In addition, both public and private shipyards will be affected by the FY 1995 Navy repair and modernization budget of \$3.2 billion, which is 15 percent more than the FY 1994 budget.

Major Shipyards

During the 1980's, the Navy commenced a long-term fleet expansion program. The goal of this program was a modern 600-ship fleet. This fleet expansion program was sharply curtailed in 1989 with the conclusion of the Cold War. The reductions in the Navy ship procurement program along with the scheduled and early decommissionings of Navy ships, combatants and auxiliary vessels, has led to a smaller active U.S. Navy fleet. The Navy's active fleet declined by 150 ships or 28 percent between the end of FY 1985 and the end of FY 1994, falling from 541 ships to 391 ships.

The U.S. Navy's shipbuilding plan for FY 1995-1999 (Table 5) includes the construction of 38 new ships costing about \$29.7 billion. The plan also includes the conversion of 13 ships. At an average of less than eight new ships per year, the Navy's five-year shipbuilding program represents a 63 percent reduction in the quantity of ships to be procured, compared with the average of 19 ships annually

for Navy programs during the 1980's. The shipbuilding plan includes an additional 10 strategic sealift new construction vessels by FY 1998. Two strategic sealift new construction vessels were contracted for in FY 1993 and two were contracted for in FY 1994, for a total of 14 sealift vessels.

National Steel and Shipbuilding Co., San Diego, CA, and Newport News Shipbuilding Co., Newport News, VA, were awarded contracts in July 1993, by the Navy's Military Sealift Command (MSC) to acquire and convert five foreign-flag commercial cargo vessels into high-speed military supply ships. The combined contracts totaled \$1.1 billion and included the detailed design for the conversion of these RO/RO ships to strategic sealift vessels. These vessels are scheduled to be redelivered between August 1995 and July 1996.

Table 5

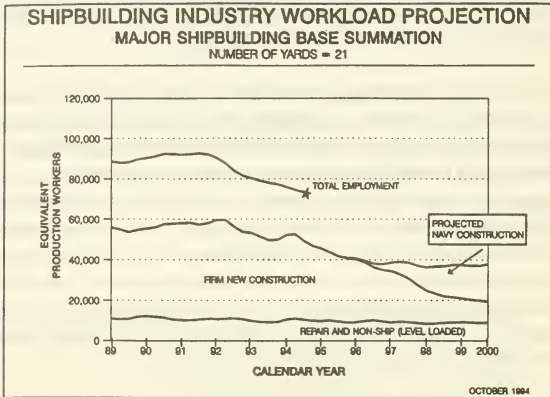
NAVY SHIPBUILDING PLAN Fiscal Years 1995 - 1999						
Ship Class	1995	1996	1997	1998	1999	TOTAL
New Construction						
CVN	1	-	-	-	-	1
SSN	-	1	-	-	-	1
DDG-51	3	3	3	3	3	15
LX	-	1	-	2	2	5
T-AGOS	-	-	1	-	1	2
T-AKR (Strategic Sealift)	2	2	4	2	-	10
MISC COMMAND	-	-	-	-	1	1
NAS	-	-	-	1	-	1
Sub-Total	6	7	8	8	7	36
Conversion/Major Overhaul						
CVN (Refueling)	-	-	-	1	-	1
T-AE (Conversion)	1	2	2	2	-	7
T-AFS (Conversion)	1	2	-	-	-	3
T-AO (Conversion)	-	-	1	-	1	2
Sub-Total	2	4	3	3	1	13
Total	8	11	11	11	8	49

The value of shipyard contracts is only about one-third of the \$29.7 billion budget; the remainder will go to such items as Government-furnished equipment placed aboard the vessels, and to Government program costs.

The primary source of employment for the major full-service shipyards, those that comprise the MSB, for the rest of the decade will continue to be activity generated by Navy shipbuilding and repair. Since mid-1992, the major shipyards have experienced a sharp decline in employment, a consequence of the sharp contraction in new Navy shipbuilding orders, the reduction in Navy repair activity, and the absence of significant commercial shipbuilding. Based on the continued reduction in the Navy's FY 1995 - 1999 shipbuilding plan, the decline in Navy ship repair activity and a paucity of new commercial shipbuilding orders, it is projected that shipyard employment will continue to decline through the end of the decade. These reductions, absent any significant orders for commercial oceangoing ships, will severely impact the remaining major U.S. shipyards.

The rising expectations of an increase in new orders for oceangoing commercial ships, 1,000 gt and over, in U.S. shipyards is not reflected in the workload projection (Chart 5). This projection reflects the manpower requirement for the confirmed shipbuilding orders as of October 1994, and the proposed Navy FY 1995 - 1999 shipbuilding plan.

Chart 5



Shipbuilding analysts generally agree in their forecasts that a significant rise in new orders for commercial ships will occur during the second half of the 1990's. This projected rise in expectations emanates from statistics regarding the current age structure of the world fleet and the projected growth in world trade. Drewry Shipping Consultants, Ltd., for example, projects that by 2001 the total replacement demand will be approximately 230 million dwt, comprising more than 14,000 vessels. Drewry also forecasts that the greatest demand will arise between 1997 and 2001, when more than 166 million dwt will be required. In addition to the replacement demand, Drewry expects that the growth in world trade will generate a requirement for an additional 300 million dwt. The bulk of this growth is expected to occur with tankers and large dry bulk carriers, gas carriers and smaller container/multipurpose vessels. (Table 6)

Table 6

**WORLD NEWBUILDING DEMAND
1992 - 2001**

Type	Replacement		Trade Growth		Total	
	DWT	%	DWT	%	DWT	%
Tanker	113.23	49.1	123.85	41.3	237.08	44.7
Dry Bulk	78.84	33.3	108.42	36.1	185.26	34.9
Chemical/Oil	2.53	1.1	5.64	1.9	8.17	1.5
Gas	1.62	0.7	8.20	2.7	9.82	1.9
Container	9.22	4.0	22.39	7.5	31.61	6.0
Other	27.07	11.8	31.56	10.5	58.65	11.0
Total	230.51		300.08		530.59	

Oil Pollution Act of 1990 (OPA-90)

Adjunct to the growing demand for replacement tonnage in the world shipping fleet is the potential impact of the Oil Pollution Act of 1990 (OPA-90) on the demand for new tanker construction. OPA-90 was signed into law on August 18, 1990 by President Bush. OPA-90 established the requirement that all tankers entering the U.S. ports by the year 2015 have double-hulls. In order to meet the double-hull objective, the new law put into place a phase-out schedule, effective January 1, 1995, for all existing single-hull tankers, based on the vessel's age and gross tonnage.

Since OPA-90 became law, U.S. shipyards have constructed a large number of double-hulled barges for ocean service and the inland waterways. Only recently has a U.S. shipyard received an order for the construction of double-hulled oceangoing tankers to meet the requirements of OPA-90. This shipyard is reportedly anticipating additional orders for their double-hulled tanker, in addition to the option attached to their current contract. Some tanker owners have solicited bids from U.S. shipyards for the possible construction of up to seven additional double-hulled oceangoing tankers, but no orders have yet been forthcoming.

As of July 1994, the U.S. domestic tanker fleet consisted of 136 petroleum tankers totaling 4.8 million gt (14.2 million dwt). As a result of OPA-90, U.S. shipyards should have significant opportunities in the years ahead to build replacement tankers or retrofit substantial replacement tanker tonnage.

It is not known how many tankers will be rebuilt, scrapped, or constructed as a result of OPA-90. What is known, according to MARAD data, is that about 1,500 tankers involved in foreign trade--or about one-third of the world's petroleum tanker fleet--enter U.S. ports.

In the 1970's there was a period of heavy building of bulk vessels in major shipbuilding nations, both tankers as well as dry bulk carriers. On a deadweight tonnage basis, 53 percent of the operational fleet was built before 1980. Many of these ships will require replacement beginning in the 1990's. In addition to normal replacement, the demand for new tankers will be spurred by the requirements of OPA-90. Major U.S. shipyards, formerly focusing on Navy work, are now gearing up for opportunities to replace the aging fleet and to build or retrofit tanker tonnage as a result of OPA-90.

Organization for Economic Cooperation and Development (OECD)

For nearly five years, the United States has worked through the Organization for Economic Cooperation and Development (OECD) to eliminate all subsidies to the shipbuilding and ship repair industry in an effort to create a "more level playing field" for the U.S. shipbuilding industry. On July 17, 1994, the United States finally reached an agreement with the world's key shipbuilding nations (including Japan, Korea and the European Union) to eliminate subsidies and other market distorting practices.

Negotiated under the auspices of the OECD, an agreement was signed in December 1994 and following ratification is expected to enter into force on

January 1, 1996. The agreement phases out virtually all direct and indirect subsidies, establishes common rules for government assisted financing, creates an injurious pricing mechanism to prevent ship dumping, and provides a binding dispute settlement mechanism. When the agreement takes effect, the Title XI program will be modified to meet its terms, which provide for a maximum repayment period of 12 years and maximum financing coverage of 80 percent.

The OECD agreement fulfills a long-sought goal of the United States which President Clinton pledged to achieve. The agreement is expected to be of great help in restoring the international competitiveness of U.S. shipyards, since it levels the playing field by requiring other countries to give up the much more substantial support they have provided to their yards, while relatively modest changes will be required in our own less subsidized programs.

National Shipbuilding and Shipyard Conversion Act of 1993

In 1993, as a follow-up to the Clinton Administration's report *Strengthening America's Shipyards: A Plan for Competing in the International Market*, Congress passed the *National Shipbuilding and Shipyard Conversion Act of 1993*. This Act amended the Title XI provisions of the Merchant Marine Act of 1936 to extend Title XI guarantees to vessels constructed, reconstructed or reconditioned in a U.S. shipyard for foreign shipowners and for shipyard modernization and improvement utilizing modern and advanced technology.

Technology that can be considered as eligible for inclusion in the categories of modern and advanced consist of: numerically controlled machine tools, robots, automated process control equipment, computerized flexible manufacturing systems, associated computer software, novel techniques and processes designed to improve shipbuilding quality, productivity and practice, and to promote sustainable development. These areas include engineering design, quality assurance, concurrent engineering, continuous process production technology,

energy efficiency, waste minimization, design for recyclability or parts reuse, inventory management, upgraded worker skills and communications with customers and suppliers. In addition, other technologies that can be included are technologies for improving shipbuilding and related industrial production which advance the state-of-the-art and the best available proven technology, techniques and processes appropriate to enhancing the productivity of shipyards.

Title XI

Pursuant to passage of the *National Shipbuilding and Shipyard Conversion Act of 1993* and restoration of Title XI program funding, MARAD has experienced a surge in Title XI applications. These applications reflect potential future work for numerous U.S. shipyards ranging from assorted barge projects to various vessels including multi-purpose cargo ships, double-hulled product tankers and a paddlewheel steamboat. Also included were four applications for shipyard modernization.

In FY 1994, a total of 12 Title XI applications, including seven for construction of new vessels or shipyard modernization and five refinancings, were approved totaling \$431 million. During the first quarter of FY 1995 MARAD received an additional nine Title XI applications and approved two totaling \$150 million. One of these latter two approvals was for the first order, since 1957, for U.S.-built ocean going commercial ships for export while the other was for a shipyard modernization project. The following table (Table 7) shows the Title XI applications approved during FY 1994 and the first quarter of FY 1995.

Table 7

FY 1994 - 1995
APPROVED TITLE XI APPLICATIONS
as of December 31, 1994

Company	Reason or Number Type of Ships	Loan Guarantee Amount (\$M)
SHIP PROJECTS		
American Steamship Company	Five Self-unloading Bulk Carriers and One Tanker (reconditioning)	\$175.6
Caneo Towing Co., Inc.	40 Double-skinned Tank Barges	\$40.7
First Tug/Barge Corp.	One Integrated Tug Barge	\$25.0
Interlake Steamship Co.	One Self-unloading Bulk Cargo Vessel	\$17.2
Oglebay Norton Co.	One Self-unloading Bulk Cargo Vessel	\$18.7
Parker Towing Company	89 River Hopper Barges and Seven River Tugs	\$8.6
Penn Barge, Inc.	Two Integrated Tug/Barges	\$26.2
Puerto Quetzal Power Corp.	Two Barge Mounted Power Plants	\$25.0
Global Industries, Ltd.	One Swath Dive Support Vessel	\$20.8
Coastal Ship, Inc.	Two Catamaran RO/ROs	\$115.9
Compania de Electricidad de Puerto Plata	One Barge Mounted Power Plant	\$34.4
Flaves Shipping Corp.	Four Product Tankers	\$133.5
SHIPYARD PROJECTS		
National Steel & Shipping Co.	Yard Modernization	\$22.7
Avondale Industries Inc.	Yard Modernization	\$15.9

In addition to the above, the U.S. shipbuilding industry is receptive to assistance which can be provided under the Defense Conversion, Reinvestment, and Transition Assistance Act of 1992. Implementation of this Act is assigned to ARPA. ARPA selected shipbuilding as one of 11 candidates for meeting future defense needs and possessing a potential for conversion to a commercial market. In ARPA's words:

"While the international shipbuilding industry is booming, the nation's shipbuilding industry is on the verge of collapse. The U.S. shipbuilding industry has been assisted by large DOD shipbuilding efforts for many years. Current and projected Navy combatant / auxiliary ship construction is insufficient to maintain the industrial shipbuilding capacity required for mobilization. This effort is intended to assist the U.S. shipyards and related industries to become competitive in international commercial markets and thereby preserve a viable shipbuilding infrastructure for defense. The effort will address innovative ship design and construction processes and ship systems technologies such as propulsion and auxiliary systems. It is expected that a number of U.S. shipyards and marine machinery manufacturers will submit proposals to ARPA for funding under this program."

To implement the Act, \$575 million was included in 1993 appropriations with \$15 million to support applied research and development for commercial shipbuilding.

Second-Tier Shipyards

The second-tier shipyards are expected to continue to boom in the years ahead. The building boom emanates from the on-going interest in the use of gaming boats as floating casinos. This trend will continue to make its mark on a variety of gaming vessel types ranging from dockside gaming barges to paddlewheelers and high tech catamarans. As the legalization of gambling continues to spread across the United States, the demand for these vessels will continue to increase.

It is expected that new orders for ferries will also continue to provide work for the second-tier shipyards. Demand will come from the continued promotion of the employment of ferries by the states for use in their tourist industries as well as an alternative to the building of additional expensive infrastructure projects such as highways and bridges. An example of the increased use of ferries can be seen in North Carolina, where the ferry division of the state's Transportation Department has a 10-year plan to expand its ferry fleet by six vessels.

Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA)

The enactment of the Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA) may have provided the single biggest Federal boost in years for the ferry business. ISTEA's purpose is to develop an efficient and environmentally sound National Intermodal Transportation System (NITS), including all forms of transit. ISTEA provides two incentives: a flexible funding program and authority for states, regions, and local agencies to decide whether funds should go for highways or

transit, including ferries. The Act specifies \$151 billion for highways, transit, and safety programs over a five-year period from FY 1993-1997 of which \$31.5 billion is for transit systems. The ferry industry will benefit from the Act's creation of a \$100 million discretionary program from the Highway Trust Fund at an 80/20 matching ratio. The Federal Government through the Department of Transportation will pick up 80 percent of the cost.

In addition to the bright prospects for new orders for the construction of gambling vessels and excursion/dinner boats, the second-tier shipyards have a healthy and diverse orderbook for a variety of smaller vessels. The shipyards are taking advantage of a booming market for towboats, drug interdiction crafts, ferries, research vessels, fireboats, petroleum and other types of barges, a variety of smaller craft, and large as well as small pleasure boats.

Data available to MARAD indicates that the second-tier shipyards are planning to continue to invest money in upgrading and improving their capital equipment. This should enable them to increase productivity and meet the expected demand for construction and repair services.

Conclusion

The U.S. shipbuilding and repair industry should continue to receive additional new construction work in the years ahead as a result of Title XI expansion to cover ships for export. The U.S. shipbuilding industry should capture a fair share of the new building tonnage required as a result of the projected growth in world trade and the projected demand for replacement tonnage. U.S. shipyards are increasingly cost competitive in the world market, as increased labor costs and changes in the exchange rates have made shipbuilding labor costs in Japan and Northern Europe significantly higher than those in the U.S.

The U.S. shipbuilding industry is making significant investments to become commercially competitive in the international market. There are many diverse factors involved in this trend: partnerships with foreign shipyards and designers to foster technology transfers; the design and introduction of new, commercially viable products; shipyard modernizations; rigorous market studies, etc. The bottom line is that suppliers, shipyards and shipyard labor are working together to facilitate the efficient and cost competitive production of quality ships and products.

With the assistance of the MARITECH program U.S. shipyards are developing additional advanced technology and productivity methods which will enable them to better compete in the world shipbuilding market. The anticipated increase in the demand for new ships for the world fleet provide an opportunity of U.S. shipyards to re-enter and establish a foothold in the foreign and domestic commercial shipbuilding markets.

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Mr. LONGLEY. Separately, do you have any information?

Admiral HERBERGER. On shipbuilding?

Mr. LONGLEY. Right; shipbuilding jobs. To what extent is MARAD concerned with the six things?

Admiral HERBERGER. Very concerned. We would have, for the record, the specifics on the numbers of jobs, the potential for the dollar trend now and if we don't get some significant commercial shipbuilding with the defense budget coming in the way it is in terms of Navy ships and other Government ships. We need to begin to step up to some significant additional commercial shipbuilding. I would provide that for the record.

[The information referred to can be obtained from the subcommittee upon request.]

Mr. LONGLEY. I would just like to end on this note. I have been fortunate to have visited probably four or five shipyards in the last several months. One of the trends that seems to be rather evident is each of them is projecting rather steep dropoffs in labor requirements attributable to declining construction of naval ships and the lack of construction of commercial shipping.

I think, frankly, we are facing a crisis. I, personally, would encourage your office to make that a very serious priority.

Admiral HERBERGER. Yes, sir.

Mr. LONGLEY. Thank you, sir. Thank you, Mr. Chairman.

Mr. BATEMAN. I thank the gentleman from Maine. Next, the gentleman from Hawaii, Mr. Abercrombie.

Mr. ABERCROMBIE. Thank you, Mr. Chairman.

Gentlemen, I am going to quote out of context here, but I believe not with any idea of trying to misrepresent the position you took. I want to cite several things to you.

Among the things that were said, if there was enough funding, enough support it would be very good. Other requirements were placed on the budget. The amounts of money that we will have available. Hopefully. These are all words and phrases that were associated with responses at various points to various members, including the chairman and the ranking minority member about what we would need in order to have the proper foundation for revitalized merchant marine both militarily useful and commercially useful. I am using the phrase "militarily useful" and "national security" that phrase as one in the same thing. I believe an active commercial merchant marine fleet is in the national security interest of the United States.

I don't believe that is a stretch. I believe I could defend that, not just in this room among like-minded people, but to any audience willing to give the time to it. After is said and done, isn't it a question then of deciding priorities?

Is the kind of fleet, both commercially and militarily useful, that we are going to have as we turn the corner on the next century, a decision that has to be made by this Congress in terms of whether it is a priority in the national defense budget? I would like your comment.

Admiral HERBERGER. Yes; absolutely.

Mr. ABERCROMBIE. There is a purpose in all of this. Admiral Quast.

Admiral QUAST. Yes, sir.

Mr. ABERCROMBIE. I'm not asking you to speak for the Pentagon or anything like that.

Admiral QUAST. I think what you are saying is hard to refute.

Mr. ABERCROMBIE. As long as I got this far then, let me go a little further and see if I can continue on from being refuted. It doesn't happen all that often in my life.

The reason I want this on the record, I am not going to quarrel with all of the things that have been said to this point because I think we are mostly on the same side here. What bothers me is I don't think the average American has a clue as to what is going on here or has been going on; doesn't have a clue.

As a result, I think what we have to do then, would you agree, if the priority question is a valid one then, that this panel has to make a recommendation first to the National Security Committee as to what it sees as its priorities in terms of acquisition?

If we have to start picking and choosing, as we apparently have to do between bombers and submarines, and one kind of armored gun system versus a V-22 helicopter, or whatever it is, pick and choose, it seems to me that if there is going to be picking and choosing then, must we not put this question of a viable militarily useful, commercially viable merchant marine into the same category?

Isn't it worthy of equal consideration with a B-2 bomber, a *Seawolf* submarine, aircraft carriers, V-22 helicopters, the acquisition of any and all and procurement of any and all acquisition of equipment, et cetera? Isn't it equal?

Admiral QUAST. I think your comment about not having a clue is right on the mark. Certainly, I spend a great deal of time and I'm sure, I don't want to speak for Admiral Herberger, but I know he is out on the speech-giving circuit trying to educate the American people about the importance of sealift.

Mr. ABERCROMBIE. I understand that.

Admiral QUAST. Sometimes you get the feeling that you are the only ones out there.

Mr. ABERCROMBIE. But I'm one of the ones that got educated. I didn't have the experience in this previously. I know that shipping is important being from Hawaii. I understand all of that. I am one of the ones that served for a time on a Merchant Marine Committee before I got on Interior. I have been on Armed Services, National Security my whole time here in the Congress. I am one of the ones that got educated.

I have been converted. The chairman and ranking minority member, are exactly correct and Mr. Cunningham is exactly correct. This is a bipartisan issue. I don't believe there is an iota of ideology involved in this unless it involves defending the interest of the United States.

If that is an ideological comment, I am perfectly happy to plead guilty to it. My question to you, gentlemen, is, Is not the issues under consideration here today the equal of any other issue under defense appropriations?

Admiral HERBERGER. Being a retired admiral I can subscribe to what you are saying. I see the sealift capability in the future, both what we are doing on the Government side to acquire a greater

kept ability and the need to retain a viable maritime industry is critical to the country.

When you look to the future and you look at the scenarios that could come up very similar to Desert Storm/Desert Shield, you are going to need a trained force in being. You are going to need to use a system that is out there in the commercial business every day. It is the most cost-effective way.

Mr. ABERCROMBIE. That would include sustainment vessels, for example.

Admiral HERBERGER. Absolutely. Our program is to retain the sustainment capability, a robust sustainment, to be able to go quickly to support the huge combatant force that will be taken by the surge force that is being built.

In the absence of that, you are going to have to wait. By waiting you may not be a deterrent force or you may not be an offensive force. I firmly believe it. You are absolutely right. The country at large does not understand this. I speak to a number of groups.

They are extremely concerned when they find out that 4 to 5 percent of our trade is being carried by American-flag vessels, the rest by foreign. We are becoming almost totally dependent on it. We need to do something to arrest that exodus. That is the centerpiece.

Mr. ABERCROMBIE. Precisely because at least we have one retired admiral and one who wants to in good order, I'm sure. My point here is that we have had discussions, and I will finish with this, Mr. Chairman. We have had discussions and had to make decisions about such things as *Seawolf* submarines and aircraft carriers, and an aircraft carrier that is going to be built at Newport News.

We are talking in the order, say between just those two items, and I am not being facetious either to you or to you, Mr. Chairman, in this. Just those two items in the defense budget, we are talking probably \$8 billion without exaggerating at all.

Yet I see arguments coming up here that don't involve half that amount of money or a quarter of that amount of money. Let's just take sustainment vessels for replacement. Without going into some of the more abstract elements of the discussion taking place here today.

You don't need to comment on this, but my concluding remark, based on these answers, Mr. Chairman, which I hope people will review as a part of this record, is that we need I believe, Mr. Chairman, you will certainly have my support. I am certain Mr. Taylor and other members of the minority on this panel, I think we need to make a vigorous, aggressive straightforward presentation to the committee as a whole as to the value of all of the issues that are involved here.

We need to put numbers on it and ships on it. I think we need to go to the mat with other members of the committee as a whole, if necessary, and with the rest of the Congress, if necessary, and with the administration, if necessary to put these issues as they have been presented into the forefront and argue that they are not only the equal, but of primary and fundamental necessity to security to the United States.

Mr. BATEMAN. I thank the gentleman for his exhortation. I take great comfort in it. Let me make clear for the record what I think is already so by asking this question of Admiral Quast.

It is the position of the Department of Defense that the Ready Reserve Fleet should be maintained as a function of the Department of Defense budget, but under the management of the Maritime Administration.

Admiral QUAST. Yes, sir; that is correct.

Mr. BATEMAN. It is the position of the Department of Defense that the operational differential payments to U.S.-flag vessels in order to preserve some remainder of a U.S.-flag fleet is supported by the Department of Defense.

Admiral QUAST. You are talking about the budget to support the RRF or to support MSP?

Mr. BATEMAN. The National Security Fleet recommendation.

Admiral QUAST. Yes, sir; it is supported by the Department of Defense.

Mr. BATEMAN. And the title XI program is supported by the Department of Defense?

Admiral QUAST. I'm not sure. I'm sure I am not sure, but I think it is a pretty good position.

Mr. BATEMAN. My spies tell me that the Secretary of the Navy at least endorsed that position this morning.

Admiral QUAST. I'm sure it is a good position. I'm still trying to retire.

Mr. BATEMAN. We do definitely want that on the record. Obviously that there is this recognition even advocacy by the Department of Defense that these maritime function are a component of our national security.

Does the gentleman from Mississippi have further questions?

Mr. TAYLOR. Mr. Chairman, this has been sort of a marathon meeting. I do have further questions. I will submit them for the record.

[No additional questions submitted.]

Mr. BATEMAN. The gentleman from Virginia, Mr. Pickett. Do you have any questions?

Mr. PICKETT. Mr. Chairman, I will submit my questions for the record since I came in late.

[No additional questions submitted.]

Mr. BATEMAN. Mr. Longley.

Mr. LONGLEY. No, Mr. Chairman.

I would compliment the Chair and the ranking member on conducting an outstanding hearing this afternoon.

Mr. BATEMAN. We thank you. Mr. Abercrombie.

Mr. ABERCROMBIE. Just one I neglected to in my passionate remarks there. I do want to ask about the Merchant Marine Academy, although I think it is pretty clear.

What has been the cost to the Federal Government to acquire and modify the State school training ships? I want to know whether the \$10 million would fund fuel and maintenance for these training ships?

Admiral HERBERGER. The request in fiscal year 1996 is \$9 million-something, nearly \$10 million, for the support of the six State academies. The largest portion of that is for the maintenance and the fuel to operate the training vessels.

In addition, there is what they call student incentive which pays for individuals that sign up. They get \$3,000 a year. They have a military Reserve obligation at the end of that period.

Mr. ABERCROMBIE. The \$10 million is sufficient in your estimation?

Admiral HERBERGER. For maintaining the level of activity that we have now; yes.

Mr. ABERCROMBIE. If the academy were close, I won't go into the transfer, would the State schools provide the quality and the quantity of the officers required to maintain this merchant marine officer quality as well as quantity?

Admiral HERBERGER. The State schools are quality institutions. My question, when I saw that recommendation is that the bulk of the support for the State academies come out of the individual States. There is no guarantee that the individual States are going to continue to be able to support at the level they have in the past.

It is my understanding talking with some of the current presidents and superintendents of those academies, there are significant cuts in the air, if you will, potential for cuts.

Mr. ABERCROMBIE. Wouldn't it be likely then that if the States faced fiscal difficulties that many of those States might conclude, look, after all this is a national responsibility?

Even though we have perhaps individual State advantages that come our way, this is something that really should be seen nationally. Then we would be in the position of having to startup all over again; right? This is not like frozen food. This is not something you put on a shelf somewhere, freeze and then take out at your convenience.

Admiral HERBERGER. It could go that way. My question right now is that a reduction in the amount of support at the Federal level as well as at the State level will have an impact on the numbers and the quantity and quite possibly the quality in the future. I think it is an inopportune time to be approaching that in light of this, what I see as an increasing need for highly qualified mariners. I am not setting up the Federal academy as higher quality than the State.

Mr. ABERCROMBIE. I didn't think that you were. I understand that.

Admiral HERBERGER. They are equivalent.

Mr. ABERCROMBIE. The question here is whether we are going to just simply transfer all of this to State responsibility or not. I think your answer is that would be unwise.

Admiral HERBERGER. I don't think it is feasible. I don't think they have the capacity to be able to absorb it without significant increase in the amount of funds needed.

Mr. ABERCROMBIE. Thank you. Mr. Chairman, I would go so far as to say that it would not be a stretch of legislative imagination to see that if we followed some of these purported recommendations where the Merchant Marine Academy is concerned, it would amount to an unfunded mandate on the States.

I am really not being facetious about that. We defect saying to the States, well, look, if you are going to do this, go ahead. If you don't it is no never mind to the Federal Government.

My own view on this then is that I think it is not warranted to look at it in the context of that particular recommendation. I think we should move ahead.

In fact, we should, if anything expand. If we are successful in getting a little more attention—not a little more, a hell of a lot more of attention paid, both in terms of funding and where we go with the fleet, we are going to need more officers.

If anything, the Merchant Marine Academy needs to be kept fully funded in order to be able to expand as needed.

Mr. BATEMAN. I thank the gentleman for his participation in the hearing this afternoon.

Gentlemen, we will have some questions that the committee would like to submit for writing. They are being formulated, some probably that will be guided by some of our discussions today. It is feasible, we would like to have an answer to them say within 2 weeks of the time you receive them.

[No additional questions submitted.]

Mr. BATEMAN. Unless there are other compelling questions that need to be raised at this point on the record, we will adjourn the hearing with our thanks to the witnesses and to the members.

[Whereupon, at 4:56 p.m., the hearing adjourned.]

ADMINISTRATION'S MARITIME SECURITY PROGRAM

HOUSE OF REPRESENTATIVES,
COMMITTEE ON NATIONAL SECURITY,
SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE,
Washington, DC, Wednesday, April 6, 1995.

The subcommittee met, pursuant to call, at 2:03 p.m. in room 2216, Rayburn House Office Building, Hon. Herbert H. Bateman (chairman of the panel) presiding.

STATEMENT OF HON. HERBERT H. BATEMAN, A REPRESENTATIVE FROM VIRGINIA, CHAIRMAN, SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE

Mr. BATEMAN. The panel will please come to order.

Welcome, ladies and gentlemen. My opening remarks will be brief today because we want to afford the maximum time for our witnesses. I want to thank them for being here.

Many of you have come from the West Coast just for this hearing, and speaking for myself, and I am sure the other Members of the panel, we want to express our sincere appreciation for your attendance and your testimony.

I understand that each of today's panels have agreed on a spokesperson, but we will, of course, afford an opportunity for any panel member to address the panel. Of necessity, such remarks would need to be brief, but feel free to amplify on your spokesperson's comments.

Last week we heard from administration witnesses on Maritime Security Act which was introduced last week by request. Both witnesses, as you would expect, expressed great urgency for action. For those of us who have faced these battles before, we know how difficult it has been and how difficult it will be to get a bill funded on the President's desk for signature.

Certainly we have gained an advantage this year in that this recent proposal by this administration is funded through the general receipts of the Treasury and not through a tonnage tax on vessels entering U.S. ports. That deletion alone improves our changes of final passage.

With that thought in mind, I would like to enter into the record at this time a letter from the President of the American Association of Port Authorities strongly supporting this year's version of maritime reform and commenting favorably on the fact that it does not rely on the tonnage tax as the funding mechanism.

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April 6, 1995

The Honorable Herb Bateman
 Chairman
 House Special Oversight Panel on Merchant Marine
 U.S. House of Representatives
 2350 Rayburn House Office Building
 Washington, D.C. 20515-4601

Dear Mr. Chairman:

Please accept this letter for the record for the April 6 hearing on H.R. 1350.

The American Association of Port Authorities (AAPA) has long supported the need for a maritime revitalization program to promote a U.S. flag fleet. In April 1992, AAPA first announced its support for the efforts toward that end, and we have consistently supported the need for a program. Although U.S. flag carriers represent, unfortunately, less than five percent of the cargo handled in U.S. ports, we recognize that the existence of a strong U.S. flag fleet in international trade provides needed competition, to the benefit of U.S. ports and shippers, as well as meeting our national security needs.

Last Congress, we expressed our concern about the use of an increase in the vessel tonnage tax to pay for the program. The public port community has already been hard hit by increases in trade taxes, which have increased prices for U.S. consumers and hurt the competitiveness of U.S. ports and exports. We are pleased that H.R. 1350 does not rely on increases in trade taxes to fund the Maritime Security Program.

Time is quickly running out, and a maritime revitalization program simply must be adopted this year in order to save our U.S. flag fleet. We will be happy to work with you and the Panel to keep H.R. 1350 on track. Thank you for your efforts in this matter.

Respectfully,

Erik Stromberg
 Erik Stromberg

RES/jcg

Mr. BATEMAN. In conclusion, let me make several initial observations. The Congress and the members of this panel have an obligation to carefully consider the administration's submission. Where we believe their proposed solution to a particular issue is appropriate, we will gladly endorse it. However, where we believe there are better approaches we will, of course, make the necessary changes.

These changes, if appropriate, will be made without regard to politics or party affiliation of the proponent. There are changes that can be made to improve this bill. There is real pain for me in the provisions of the administration's bill that removes the U.S. bill requirement for operators who are provided ODS payments.

We should use our ingenuity to develop legislation that will aid American shipbuilders in their struggle to survive the austere naval shipbuilding construction program of the next several years. Like our U.S. flag, U.S. manned merchant marine domestic shipbuilding is a linchpin of national security.

To the witnesses appearing today, this is your opportunity to offer your views and your expertise on how we might produce a bill that all interests can embrace.

I would like to now recognize the gentleman from Mississippi, the ranking member of the panel, my friend Congressman Gene Taylor for any comments he may wish to make.

Mr. TAYLOR. Thank you, Mr. Chairman.

I would like to thank you, my fellow members of the panel and our distinguished witnesses, for participating in today's hearing on the administration's maritime security program. First, I wish to express my support for the U.S. flag fleet and the American merchant seaman who crew the vessels that are so important to our national security. However, as I have previously mentioned to some of the panels who will be testifying before this proposal, I do not under any circumstances support providing U.S. taxpayer subsidies for foreign-built ships.

Having said that, I welcome our guest here today. I sincerely look forward to hearing what they have to say. I also look forward to the day when you return to buying America-made ships.

I would also like to offer a particular welcome to a former great member of the Merchant Marine Committee, the iron lady of the U.S. maritime industry, Congresswoman Helen Bentley.

Thank you, Mr. Chairman.

Mr. BATEMAN. Thank you, Gene, and thank you for recognizing our former and very distinguished colleague.

Helen, we are always delighted to have you in our proceedings.

Now, the first panel of witnesses consists of John W. Snow, the Chairman and CEO of CSX Corp.; John M. Lillie, the President and CEO and Chairman of American President Companies, Limited; William P. Verdon, Senior Vice President and General Counsel for Crowley Maritime Corp.; and Erik F. Johnsen, President and CEO of Central Gulf Lines and Waterman Steamship.

Is there any Member of the panel who would like to make an opening statement?

There being none, Mr. Snow, I understand you are going to be the opening spokesperson.

STATEMENT OF JOHN W. SNOW, CHAIRMAN AND CEO, CSX CORPORATION

Mr. SNOW. Thank you, Mr. Chairman. With me are John Lillie, of American President, Bill Verdon of Crowley, and Eric Johnsen from Central Gulf & Waterman.

We have prepared a lengthy statement which I would ask to be entered into the record, and I will try summarize it briefly.

Mr. BATEMAN. We will happily enter that statement in the record, Mr. Snow, and you may proceed.

Mr. SNOW. Let me respond to both you and Congressman Taylor by saying that we share your sense of urgency about moving forward with real changes in U.S. maritime policy. So that on the one hand we can continue to be competitive and become more competitive. And, Congressman Taylor, I too, like you, look forward to the day when we will be in the position to be competitive and the shipyards will be competitive and we will be buying ships from the American shipyards because we share your concern about the shipyards and the state of that industry.

Let me say, Mr. Chairman, first of all that we deeply appreciated your holding this hearing so early in the session. In the past, we have had hearings but often they have come late in the session, which made legislative action on this important matter difficult to achieve.

This panel's interest in the whole subject of the revitalization of the American maritime industry, including the shipyards, is vitally important to us. And it is our concern that unless we act soon, the decay and the decline that is all so evident will simply continue, and that there are low-cost, market-oriented, deregulation-based approaches consistent with what I take to be the new political dynamics of the country that will allow this industry to become more competitive. Arrest the decay, arrest the decline and put us on a fundamentally different course for the future.

We have four key points to make. First of all, the U.S.-flag liner fleet, and you know this, provides important national security benefits at low cost. We see the private sector, the private sector operating maritime industry as an adjunct, an important adjunct to national security that can provide necessary sealift at costs far below the costs of organic capacity through the Defense Department.

Second, we think that the U.S. flag fleet provides important benefits to the Nation going above and beyond national security. It makes U.S. importers and U.S. exporters far more competitive.

We dread to see the day where the U.S. shippers are dependent upon foreign-flag carriers for all of their commerce into and out of this country. And unless action is taken, that day is not too far in the future.

Third, I think it is important to recognize that despite all of the good intentions that lie behind them, present policies simply are not working. And the best evidence of that, Mr. Chairman and members of the panel, is simply the facts of the decline in the U.S.-flag fleet over the past 30 or 40 years. They speak volumes about the failure of existing policies.

And fourth—and this is critical to the discussion that has to ensue as you consider legislation—we believe that a low-cost, deregulatory-based approach or program of long decay and decline.

At the outset, let me note that this has really been a bipartisan initiative we, the four of us, have been involved in for now over 4 years. It has had support and beyond that really, it has had support of the Reagan administration, it had the support of the Bush administration and it has had the strong support now from the Clinton administration.

In particular, I would like to call attention to the role of Andy Card, the Secretary of Transportation under President Bush, who really took this issue on and gave it his best efforts. And the legislation that we are working with today in many ways builds on and derives from Secretary Card's initiative.

Let me try and just briefly build on these four points. First, with respect to defense, I think the gulf war is a fitting demonstration of the role of the U.S.-flag fleet plays in contributing to our Nation's national security. There, I think, the record shows we made a huge contribution. I think the Defense Department will testify to that. Eighty thousand containers is what we moved. That is an awful lot of containers in a short period of time. And we moved those and additional noncontainerized cargoes to the Persian Gulf area promptly and at reasonable costs and effectively in accordance with sealift requirements.

Our crews, the U.S.-flag crews that man our ships, performed admirably and well as they have in every single national emergency. U.S. citizen crews did not balk at entering the Persian Gulf. Some foreign crews did.

I think the issue here is if we rely on foreign crews, what assurance do we have that those crews will man the ships going into theaters where their own interests are hostile to the interests of the United States? A big issue, I think, Mr. Chairman.

Beyond the example of the gulf war, let me recite, just say a few other basic ways that the American liner fleet furthers our national security interests. It is the crew of our vessels that provide the pool of mariners. And this, I think, is the critical issue: The commercial fleets of the United States provide the pool of mariners which operate the DOD reserve vessels.

And so as the pool of U.S.-flag fleet and as the role of the U.S.-flag fleet in world markets dwindles, the reserve of pool of mariners from which the DOD can draw declines and that present a grave threat, long-term to manning the reserve fleet. If there is no U.S.-flag liner fleet, the maritime pool eventually disappears and with it the capacity of DOD to man the reserve fleets. I think that just has to be underscored as a fundamental reason why action is needed and needed soon.

Beyond that, of course, we feel we carry the cargo cost effectively in peacetime as well as in emergencies, and our vessels can assist in surge as well as sustainment. Our companies offer a full line of logistic services. It is not just port to port. But it is a full line of computers and information systems and logistics and distribution services and terminals as well as the ships themselves that the DOD can take advantage of and does take advantage of.

And finally, let me say on this score, it would cost the government in our estimation a great deal more than the cost of the proposal program to replicate the assets we can now make available at very low costs.

So this, in effect, is a program to rely on the private sector effectively to maintain an important infrastructure of the United States at a low cost, at a lower cost than if that infrastructure was provided through Federal action independently of the private sector.

The economic benefits I mentioned. Let me comment there. World trade is obviously a growth activity, one in which the United States needs to participate.

World trade depends on shipping and container fleets. Today, our container fleets represent only some 5 to 7 percent of our export and import industries. The U.S. can either be an important participant in this activity or not. If we do by making the modest investment we have been talking about in the U.S. liner fleet, there is a huge payoff in terms of jobs, in terms of tax revenues, in terms of foreign currency, in terms of foreign exchange.

The third point, present law simply is not working, born of good intentions, but it is a failure. It is not accomplishing the end objective of that law which was to sustain and enhance a vigorous and strong U.S. flag fleet. We simply are not getting that objective, Mr. Chairman. And if we stay on the course we are on, we are going to have no U.S.-flag fleet.

And so we are confronted with this fundamental issue, cross-roads type of issue, which way do we go? And we would suggest, as I said earlier, that changing the current system and adopting the low-cost deregulatory sort of approach that is contained in the administration bill offers great promise here.

Let me cite a few facts. As recently as fiscal year 1984, the Treasury spent over \$400 million on the operating differential subsidy program. Under the plan that you are reviewing in fiscal year 1998, we would spend \$100 million for the same function, a 75-percent cost cut in current dollars, obviously more when inflation is taken into account. We think it is a bargain. And the per ship per year levels are also way, way down.

So this seems to us to be consistent with cost-effective government, with using the private sector, with deregulation, with a lot of the important forces that are working their way through the Congress and really through the country.

Let me mention a few of the details of the program and offer some thoughts. This is a lean program, but we think it is workable. If it gets any leaner, I am not sure it would be workable. In such a lean program, it is important that there are not an awful lot of strings because, after all, what we are talking about here is allowing the U.S.-flag fleets to compete against carriers in the rest of the world, China and Japan and Europe and Asia, which are using entirely—fleets entirely made up of foreign crews, and we have to be in the long-term competitive with those ships and those crews and those companies and those competitors if we are going to remain viable.

And for that reason, it seems to us that it is important to recognize that the underlying objective here is to have a competitive fleet. And to have a competitive fleet, we have to have the minimum restrictions necessary to implement the program.

I would strongly urge you to think about limiting the restrictions. Today, the ODS program works with a number of restrictions, re-

strictions that really are counterproductive in terms of having a viable U.S.-flag fleet.

That is really our testimony. We think there is an opportunity here to arrest the decline, to put us on a new course, to do so at low cost to augment national security, and to revitalize this industry that has played such an important and historic role in the life of this Nation.

Thank you, Mr. Chairman. Maybe Mr. Lillie and my colleagues would like to add a thought or two.

[The prepared statement of Mr. Snow follows:]

Joint Statement

of

AMERICAN PRESIDENT LINES, LTD.
CENTRAL GULF LINES, INC.
CROWLEY MARITIME CORPORATION
CSX CORPORATION/SEA-LAND SERVICE, INC.
FARRELL LINES, INC.
LYKES BROS. STEAMSHIP CO., INC.
MATSON NAVIGATION COMPANY, INC.
TOTEM RESOURCES CORPORATION
WATERMAN STEAMSHIP CORPORATION

Supporting

PROMPT ENACTMENT OF LEGISLATION
TO REVITALIZE THE
UNITED STATES-FLAG LINER FLEET

before the

PANEL ON THE MERCHANT MARINE
COMMITTEE ON NATIONAL SECURITY
UNITED STATES HOUSE OF REPRESENTATIVES

WASHINGTON, D.C.

April 6, 1995

JOINT STATEMENT OF
 AMERICAN PRESIDENT LINES, LTD; CENTRAL GULF LINES, INC.;
 CROWLEY MARITIME CORPORATION; CSX CORPORATION/SEA-LAND SERVICE, INC.;
 FARRELL LINES, INC.; LYKES BROS. STEAMSHIP CO., INC.;
 MATSON NAVIGATION COMPANY, INC.; TOTEM RESOURCES CORPORATION; AND
 WATERMAN STEAMSHIP CORPORATION

Mr. Chairman and Members of the Panel:

We appear before you today to urge prompt enactment of long overdue legislation to revitalize the United States-flag liner fleet. Such legislation is essential to the public interest in general, and to our national security in particular. This can be done consistent with today's broad public consensus for reducing government spending and eliminating regulatory burdens.

We are very pleased that you have scheduled this hearing so early in the session, Mr. Chairman. The interest in this issue shown by you and your colleagues is deeply appreciated. We are committed to working with this panel, others in the Congress, and with the Administration, to turn that interest into enactment of an historic maritime revitalization bill, together with appropriations for it, by September 30 of this year.

As we meet here today, the existing program of support for the U.S.-flag liner fleet is winding down. Today, U.S.-flag operators, whether under the existing program or not, are not on a level playing field with foreign-flag competitors. We have a choice. We can either do nothing or replace the old program with a better one.

If we do nothing, American flag vessels and their American crews will fast become extinct in international liner trades. A fundamental part of our national sealift capability will be lost.

Instead, we should replace the old program with an improved and modern one, one which is highly cost efficient and deregulatory. If we do this, we will have finally taken a critical step forward in fostering an American liner fleet which is able to compete in world markets and provide very substantial sealift in support of our armed forces.

In taking this position, Mr. Chairman, we stress that American liner companies are highly capable. As Admiral Herberger noted in his testimony before you last week, the U.S.-flag liner fleet has been a world leader, with the companies ushering in technological innovation after innovation.

But, even with that, our laws handicap us against our competitors. And that has been recognized on a bipartisan basis by the last three Administrations. The Clinton Administration, like the Reagan and Bush Administrations before it, is recommending a continued program commitment to the

U.S.-flag liner fleet combined with deregulation. We agree that a new, deregulatory program is what is required. We urge you to enact such a program promptly.

In support of that position, in the balance of our statement we will emphasize just a few key points.

OVERVIEW OF TESTIMONY

1. The U.S.-Flag Liner Fleet Provides Important Defense Benefits. The U.S.-flag liner fleet and its U.S. citizen crews are valuable, cost-effective, fundamental assets to the national defense. Government support for the U.S.-flag liner fleet is a sound investment. It ensures the availability of U.S.-flag vessels and U.S. citizen mariners -- both in times of need and in peacetime. And it ensures the availability of those assets at a fraction of the cost that would be required if the Government tried to acquire and operate them itself.

2. The U.S.-Flag Liner Fleet Provides Economic Benefits. While providing important defense benefits, a U.S.-flag liner fleet also provides important economic benefits to the nation.

3. Reform of Present Law Is Needed. An overhaul of our nation's promotional laws for liner vessels is needed. We have years of experience with present promotional laws, and have seen how burdensome statutory and regulatory requirements disadvantage U.S.-flag operations in today's world of intense international competition. New legislation must correct that. Our laws must not place American liner companies at a competitive disadvantage for operating U.S.-flag vessels. Otherwise, it only stands to reason that at least some will be forced to find other ways to operate competitively, or not operate at all. And, in that case, the defense and economic benefits of the U.S.-flag fleet would be lost to the nation.

4. A Low Cost, Deregulatory Program Is The Solution. The significant benefits of a U.S.-flag liner fleet can be obtained with a modern program that reduces government costs -- both per vessel and program wide -- compared with present and historical levels, while eliminating requirements which handicap U.S.-flag operators compared to their foreign-flag competitors. Low cost with deregulation is the basic thrust of the Administration's proposal. While we think it essential that the Administration's proposal be modified in a number of areas, that proposal is on the right track.

THE U.S.-FLAG LINER FLEET AND U.S.-CITIZEN CREWS PROVIDE NATIONAL SECURITY BENEFITS FOR THE NATION

The remarkable logistics feat of Operations Desert Shield and Desert Storm demonstrated yet again that the nation needs a U.S.-flag merchant fleet in times of national emergency. In the Gulf War, as in most major operations, the overwhelming majority of supplies moved by vessel, not air. In practice, this means that the privately owned and operated U.S.-flag liner fleet is vital to our national security.

Although the Persian Gulf conflict was a situation in which the United States enjoyed broad international support, 81 percent of the dry cargo moved to the region on U.S.-flag vessels. U.S.-flag liner carriers represented here transported almost 80,000 TEUs of containerized cargo, plus significant amounts of non-containerized cargo moved on break-bulk, roll-on\roll-off, and LASH vessels. We demonstrated to the world how military supplies could be moved effectively and cost-efficiently by U.S.-flag commercial vessels, operating in large part on commercial service routes.

Moreover, in response to the Defense Department's request, we provided more than ships. We added a complete world-wide intermodal shipping system, including experienced management teams, trained mariners, state-of-the-art port facilities, logistics and information systems and services, containers and equipment.

This commercial fleet also enables the Defense Department's own vessels to serve more effectively. This is because an active commercial fleet provides the mariner pool to crew vessels drawn from the government's reserve fleets during emergencies.

We also want to point out that American seafarers have proudly supported U.S. forces during virtually every military conflict in the history of the country. They have always responded when asked. During the Gulf War, there were incidents where some foreign-flag crews balked at bringing their ships and cargoes into the Persian Gulf -- this despite the overwhelming international support for that mission. It is readily conceivable, as you noted at last week's hearing, Mr. Chairman, that future U.S. military missions may not enjoy such wide international support. To ensure the most reliable support for our forces in such instances, it is important for our nation to implement policies which promote a fleet of U.S.-flag liner vessels, with U.S. citizen crews.

Let us briefly note other ways in which U.S.-flag liner vessels help meet defense needs.

- U.S.-flag vessels carry DOD cargo during peacetime in a cost-effective manner.
- During both emergencies and peacetime, American liner operators provide services far beyond ocean transportation. Such services include a complete intermodal shipping system and its elements, including experienced management teams, state-of-the-art port facilities, logistics and information services, containers, LASH barges and other equipment. This allows the military to utilize seamless transportation and to focus on military issues, rather than have to separately assemble water and land transportation.
- American operators provide surge as well as sustainment support. Our vessels and systems are in place and moving all the time. We can assist right away, not just in sustainment. Recent military exercises have proven the effectiveness of U.S.-flag liner operators in carrying combat support equipment for the military. Today there is a shortfall in surge capacity, increasing the attractiveness of efforts to retain the capabilities of the U.S.-flag liner fleet.

It is also important to remember that our fleet of liner ships, the complementary intermodal network already in place and ready around the globe, the large personnel pool which the companies support, and the rest of the companies' distribution and logistics systems, are kept modern and readily available at the expense of the private sector. Billions of dollars in capital have been invested and billions are spent annually operating these systems. For the taxpayer, a very modest support program which ensures the nation's continued access to these ships and systems for security purposes is immeasurably less expensive than having the Government acquire and maintain or operate similar assets of its own -- not even factoring in the problems and cost of finding crews and administering nationalized vessels. The cost effectiveness to our nation of employing commercial U.S.-flag liner vessels to carry DOD cargo, both in emergencies and in peacetime, was underscored in a report completed just last month by Mercer Management Consulting. We have provided a copy of that study to the Committee staff.

ECONOMIC BENEFITS OF A U.S.-FLAG LINER FLEET

We want to be clear that the U.S.-flag liner fleet provides economic as well as military benefits to the nation.

As we all know, world trade is growing and most trade moves by ship. So, support for U.S.-flag liner vessels represents an investment which helps ensure U.S. participation in a world industry which is growing, not declining.

In addition, this fleet ensures that America's peacetime commerce will never become fully captive to foreign shipping. The presence of U.S.-flag vessels on our major trade routes helps ensure that the delivered price of American exports and imports is not determined unilaterally by foreign carriers, which in many instances are affiliated with foreign producers of their national governments. Secretary Peña has noted that it would be unthinkable for the U.S. to jeopardize its national economic interests by not having any U.S.-flag vessels to carry a portion of our country's imports and exports.

In addition, the use of United States-flag liner vessels helps reduce the U.S. deficit in foreign trade accounts. The employment of thousands of Americans at sea and in company operations throughout the country boosts the economy and tax revenues. That investments in the U.S.-flag liner fleet yield these kinds of benefits was confirmed by a recent study by Nathan Associates. That study found that, in 1992, the ODS program generated, directly and indirectly, 31,000 jobs, \$1.6 billion in household earnings, \$268 million in federal income tax revenues, and \$900 million in foreign exchange. Even if one were not to attribute all of these benefits to the program, these findings broadly confirm that there are economic as well as defense benefits from investment in a U.S.-flag liner program.

THE NEED FOR REFORM: DIFFICULTIES COMPETING UNDER THE U.S. FLAG

Not too many years ago, the carriers participating in this statement were only some of many companies operating United States-flag liner vessels. Now we are virtually all that are left. Other companies have not been able to withstand the increasingly intense foreign-flag competition.

But we are competitors, Mr. Chairman. We are still here. We have managed to beat the odds even though, as U.S.-flag carriers, we are not able to operate on a level playing field with our foreign-flag competitors. There are a number of key areas of difference between our collective costs and those of our foreign competitors. Let us briefly explain some of these problems.

Operating and Capital Costs

As we have made clear, a tremendous advantage of U.S.-flag vessels to the nation is the employment of U.S. citizen crews.

Our U.S.-flag liner vessels are in competition with vessels that have far lower operating costs. The operating-differential subsidy (ODS) contracts of subsidized U.S.-flag carriers essentially provide parity against low wage compensation, but those contracts expire in 1996 and 1997. For the unsubsidized carriers, the wage difference with foreign-flag vessels is a major disadvantage right now and has been for years.

Vessel capital costs are at least as critical an issue in ensuring the international competitiveness of the U.S.-flag liner fleet. Any restrictions on the ability to acquire market priced vessels puts a carrier at an unacceptable disadvantage to its competitors. Our shareholders and the financial community will not allow us to do that. Yet today's ODS program effectively denies carriers the opportunity to purchase competitively priced ships for use in the program.

So, the current system of "promotional" laws leaves both unsubsidized and subsidized U.S.-flag carriers at a competitive disadvantage to their foreign-flag competitors.

Tax and Other Gaps

U.S.-based liner companies are subject to significantly higher taxes than their foreign-based counterparts. In testimony two years ago to the Merchant Marine and Fisheries Committee, APL and Sea-Land submitted data showing that, as a result of shipping income tax exemptions, deferral devices, and accelerated depreciation, many of our foreign-flag competitors pay virtually no income taxes (neither do their crew, under many foreign tax regimes). Yet, here at home, even in our unprofitable years, we are subject to the Alternative Minimum Tax. Consequently, U.S.-flag operators must generate more revenue in the marketplace than their competitors in order to earn the same amount for reinvestment in the business or distribution to shareholders. Similarly, various vessel rules regarding inspection, health and equipment increase the costs of U.S.-flag compared to foreign-flag vessels. We are not here today to seek maritime tax reform legislation (though it would be a great help) or to change vessel rules. We note these gaps, however, to underscore the urgent need to enact a

modern program for the U.S.-flag liner fleet to enable us to compete with foreign-flag operators on a more reasonable basis.

In short, Mr. Chairman, for those and other reasons U.S. carriers are in a very tough position. The problems are there, they are significant, and they are caused by U.S. government policies. Without legislation which gives U.S.-flag operations a fair chance to compete, the decline in the U.S.-flag fleet can only continue.

THE NEEDED LEGISLATIVE RESPONSE -- A LOW COST, DEREGULATORY PROGRAM

As we said at the outset, Mr. Chairman, the way to

- respond to the deficiencies of the present law, while
- securing for the nation the defense and economic benefits of a U.S.-flag liner fleet, while
- remaining consistent with broad trends to reduce spending and regulations

is to establish a low cost, deregulatory program of support for U.S.-flag liner vessels.

We believe that the basic approach staked out by the Administration's proposal, introduced by request as H.R. 1350, is a good beginning. Let us be clear, however, we think it essential that the Administration proposal be modified in a number of ways; both the House and Senate last year found it essential to make changes to the Administration proposal. While changes are necessary, Mr. Chairman, we are optimistic that they can be achieved, as many of them are fairly technical. We look forward to working with you and your staff to achieve essential changes.

Let us offer today just a few broad comments on aspects of the Administration's bill.

FUNDING

The Administration has proposed a program of \$100 million dollars per year for 10 years. Payments would commence at \$2.5 million per ship per year for FYs 1996-1998 and drop to \$2 million per ship per year for FYs 1999-2005. We would prefer a larger, longer program but, recognizing today's pressures on government spending, we support a program at this level.

It is important to keep in mind, Mr. Chairman, how low these levels are measured against past expenditures for the ODS program. In FY 1984 the appropriation to liquidate ODS obligations was

over \$401 million. If you assume enactment of a program funded at the Administration's levels, in FY 1998, when there will be essentially no more ODS payments for liner vessels, total outlays will be \$100 million. This is a decline of 75 percent in current dollars, compared to 1984, for the same function. When inflation is considered, this represents a decline of roughly 90 percent from 1984 to 1998.

Beyond total spending levels, the expenditures per vessel under the Administration's proposed Maritime Security Act will be roughly one-third less per vessel per year compared to ODS payments.

These are huge reductions, Mr. Chairman, by any standard.

We note with approval that this year the Administration would fund the program out of the General Fund of the Treasury, which has always been the source of funds for ODS payments. One key difference between the proposed new program and ODS is that the new program must be supported by appropriation of budget authority. Under the ODS program, the agency was able to bind the Government by entering into contracts; appropriations would be provided not to create authority to pay carriers but to liquidate legal obligations to pay. Let us be clear. In this narrow regard the former program provided a commitment to the carrier that the Government was offering a viable program, the kind of program that can readily attract major new investment. The ODS program was enacted in 1936, however, before today's budget rules and concerns.

So, we understand the approach taken in H.R. 1350, of authorization for annual appropriations. There are two key things that Congress must do, however, to be sure that this approach can yield an acceptable liner program for the American people.

First, there must be appropriations. We urge you, Mr. Chairman, not only to work for enactment of needed authorizing legislation, but to work with your colleagues on the Appropriations Committee to obtain the equally needed appropriations. Second, we must be clear that the companies are treated fairly and given the right to reflag if a funded program does not emerge from Congress in any year. Our companies cannot bring assets into this program if the program details in any way constitute a commitment to an unfunded program, rather than an opportunity to compete in world markets.

PROGRAM ELEMENTS AND REQUIREMENTS

Let us turn now to just a few comments about elements of the program as proposed by the Administration. Many of its aspects are commendable. It starts to eliminate a great deal of the red tape and unnecessary restrictions associated with the ODS program and includes solid reforms.

For example, vessels under the new program are not subject to so-called trade route regulation -- restrictions on what ports they can call and how often. The bill includes a considered approach to the important issue of service in domestic offshore trades. That approach balances the views of purely domestic carriers and domestic carriers with international operations, providing for program carriers engaged in foreign commerce to continue in domestic trades without unfair impact on unsubsidized pure domestic carriers. It also provides for multi-year contracts with carriers even though the contracts are subject to appropriations.

Ensuring Competitive Options -- Program Eligibility

A key aspect of any program is a clear delineation of the eligibility requirements for participation in the program. There is diversity within the liner segment of the U.S.-flag industry -- fleets are of different ages and types, with vessels designed to serve the demands of different markets and different port and internal transport infrastructures. Yet all are militarily useful.

The Administration's proposed Maritime Security Fleet reflects particular interest in vessels under 15 years of age. Many somewhat older vessels, however, are well maintained and can well serve national interests. We have felt for some time that a bill should provide all U.S.-flag liner operators a reasonable chance to participate in the program on a voluntary basis. We do not feel that the Administration's proposal fully provides that flexibility; we will recommend amendments to make clear that containerships, ro-ro vessels, and LASH (Lighter Aboard Ship) vessels will be eligible for participation in the program.

Ensuring Competitive Options - Mixed Fleets

Competitive operation of a liner service requires that management have operational flexibility. If strings are attached to program participation which deny that flexibility, U.S.-flag vessel operations are handicapped and discouraged. Simply, a company would lose flexibility -- i.e., competitiveness -- because it operated U.S.-flag ships under a program.

Mixed fleets (companies operating both U.S.- and foreign-flag vessels) is a key flexibility issue. For a vessel operator to commit to using U.S.-flag vessels as much as possible, that operator has to know that making that choice does not become a "trap" leading to non-competitive restrictions on its operations.

In today's world of liner trade, competition is waged not just between vessels, but between fleets of vessels and intermodal systems in numerous global markets. A company with U.S.-flag vessels is in commercial competition with companies using fleets of all foreign-flag vessels. The company with U.S.-flag vessels has to know that, if it needs to respond to a commercial competitive situation, it can do so, even if that means some use of foreign-flag vessels. And it needs to know that in part because, for the foreseeable future, it seems unrealistic to believe that there would be adequate funding for many additional U.S.-flag vessels.

The Administration has shown understanding that there needs to be freedom in this area, but its proposal does not do enough to give a company operating a mix of U.S.-flag program vessels and foreign-flag vessels as much flexibility as the all foreign-flag competitor. For many of us, appropriate change to H.R. 1350 in this area will be essential.

A somewhat related point is whether the program provides operators with flexibility to effectively use U.S.-flag vessels which are not included in the program. On this, the Administration bill partially achieves what is needed. It provides that if Congress does not appropriate funds and a vessel enrolled in the new program is not paid, the carrier has the right to reflag the vessel. It is essential, and a matter of fairness, that this approach be extended to liner vessels that are not participating in the new program. Such a provision was passed by the House of Representatives in the last Congress.

Summary, Program Requirements

As noted at the outset, we believe that the Administration's bill requires improvement in a number of areas. The key point that we want to make today about modifications to H.R. 1350 is not the particulars of our concerns, but the underlying reason we will be advancing them. At all times, but particularly under a very lean payment schedule, the program must be highly workable from the carrier standpoint. It must provide certainty, and preclude unintended regulatory restrictions. If the program does not meet these tests, the goal of leveling the playing field with foreign carriers will be undercut, the program will become less attractive to U.S.-flag liner operators, and it will not achieve its public interest objective.

But if it is -- and we are confident it can -- then a workable program of support for U.S.-flag liner carriers will be achieved, preserving for the nation the valuable national security services and other benefits that fleet provides.

CONCLUSION

Mr. Chairman, prompt passage of this long overdue legislation would well serve national defense and economic interests. This can be done consistent with today's demands for lean programs and deregulation. That there are public benefits to be gained from action in this area is confirmed by the fact that the Clinton, Bush, and Reagan Administrations have all sought such legislation. This is the year, however, to bring that long term, bipartisan effort to a successful conclusion. We pledge to work with this panel and the Congress to achieve enactment of this legislation, and appropriations for it, by September 30.

Thank you for the opportunity to appear before you today. At this time, we'd be pleased to respond to any questions you may have.

* * * * *

Mr. BATEMAN. Yes; would be glad to hear from Mr. Lillie or Mr. Verdon or Mr. Johnsen in that sequence, if any of you care to amplify.

STATEMENT OF JOHN M. LILLIE, PRESIDENT, CEO AND CHAIRMAN, AMERICAN PRESIDENT COMPANIES, LIMITED

Mr. LILLIE. Thank you, Mr. Chairman, and thank you, Mr. Snow, for your opening remarks on our behalf.

I wanted to take a moment this morning to remind the Members of the relationship between the preservation of the Shipping Act of 1994 and the maritime security program that we are discussing today.

I especially want to thank all of the members of the panel who have expressed their interest in this matter, particularly you, Mr. Chairman, for your personal involvement in emphasizing the national security importance of the Shipping Act both during and after the maritime transportation subcommittee hearings on the act.

In addition, I want to thank the members of the panel who have written Chairmen Shuster and Coble about these matters and for the many expressions from members of the panel of concern and interest in this matter.

As you know, the Shipping Act is essential to our ability to do business as an American company. If the act is changed in any respect to give a greater competitive advantage to our foreign competitors, or to undermine the stable investment environment that is necessary to ensure private investment in the U.S. liner fleet, our ability to remain an American company is put at risk.

Our company and its predecessors have operated for 147 years under the U.S.-flag serving our customers and serving our Nation, an important part of the success of that operation has been the qualified and highly dedicated group of mariners who serve on our vessels.

I think the matter that is before us today is, will our Nation continue to make an investment in these highly qualified people for security and commercial reasons?

Thank you very much, Mr. Chairman.

Mr. BATEMAN. Thank you.

Mr. Verdon.

STATEMENT OF WILLIAM P. VERDON, SENIOR VICE PRESIDENT AND GENERAL COUNSEL, CROWLEY MARITIME CORPORATION

Mr. VERDON. Thank you, Mr. Chairman.

I just would like to add a few words to Mr. Snow's remarks. I think they were emphatically stated and we all support them, but I would like to add the point that we have been doing this, John mentioned, for years. Actually it was 15 years ago when we had our first hearing on promotional reform and the only thing that has really changed is that some of us are not here any longer or those that are a little older or grayer.

The fact remains that we have failed every year for 14 years to get this over the goal line, and the reason we have failed is that in our own house we could not get order. The carriers were divided

for many, many years as to how they wanted to get a reform program put together. In other years, it was the House that was against us. In other years, it was some pieces of the Senate that were against us. In other years, it was the administration that was lukewarm or not warm at all.

Finally, we are at a point now, I think, that the carriers clearly are united. The unions are supportive and united. The House passed essentially the same kind of bill overwhelmingly last year. The Senate is supportive. And now we have the administration putting the bill forward. So I think the time for all the talk is finished and we really need a sense of urgency for the Congress to now say, let's just do it.

It used to be we would come up and argue points with the Congress. There is nothing really left to argue. Everyone is much agreed. Nobody is against the program. There are some little nits that have to be cleaned up maybe, but we are ready to go and I think it is going to take an awakening and awareness that this is the time to do it, because if we do not do it this time, and I know it sounds maybe like Chicken Little, the sky is falling down, because we have said it before, but if it is not done this time it is a little different.

There are carriers who have made application to go foreign-flag because they no longer can stay American flag without support. There are other carriers who are getting ready to make those applications. There is an attack on the Shipping Act of 1984, and if you look back 15 years ago, this table had to be a lot bigger because there were 12 and 14 and 15 carriers here. Today there are four of us with two or three others who are not here but supportive of us.

So I think now is the time to act and if there is no dispute, let's get on with it and get it over with.

With that in mind, we thank you very much for your support in bringing this to the forefront.

Thank you.

Mr. BATEMAN. Mr. Johnsen.

STATEMENT OF ERIK F. JOHNSEN, PRESIDENT AND CEO, CENTRAL GULF LINES, INC.

Mr. JOHNSEN. Mr. Chairman, thank you for this opportunity, and the panel and the committee, for allowing us to appear before you today.

I support Mr. Snow's statement. As he stated, this is a unified approach that we have put forward. I guess I happen to be the one on the panel that has been in this maritime field for the longest period. I started as a seaman, and, therefore, I have been on both sides of the fence. I have seen what has happened for many years. And basically, what we have is a determination as to whether or not we and the U.S. flag can be competitive internationally. That is the name of the game. We think that this program will, indeed, give us that opportunity.

As Mr. Snow correctly pointed out, there is a reduction from the past under the old ODS program of some 75 percent. This will require the unions and the operators to get together and say, Let's

cut costs. This is the name of the game and we are prepared to do it.

As I look past the last 40 years, we have had the continual call upon this industry, which I think is unusual and a unique situation, that every time there has been a flareup, there has been an expansion and then a consideration. Korea, Suez, Vietnam, Desert Storm, in each case, this industry has been called upon to expand their numbers and contract. They have built a lot of ships in U.S. shipyards.

We have built a lot ourselves in Avondale. We are located in New Orleans and we have done work with those yards. We believe that if they are given the opportunity to be competitive, they have stated in testimony before your committees, that they can be competitive. We are certainly supportive of giving more business to U.S. shipyards.

We do not want to have it understood that we are, quote, "subsidizing" a foreign-built ship. What we are saying is we need to have the assistance to equate us from the point of view of the sailors to equal cost with our competition. That is what we are looking for.

We have been innovative. But when you start a race and you start with everybody else getting a head start on you, it is pretty hard to win. We are prepared to work, and I am satisfied the union officials here will say the same, to work together to get our costs in line and to merit the support that you will give us.

Desert Storm was another example. We have a number of LASH vessels. They are militarily useful vessels. They were there. They were there throughout the entire Desert Storm conflagration.

With that, I thank you very much. And I am being a little redundant from the others, but I think it is something that is important for you to understand that we are here to say that we also want to get our costs more and more in line together with our union counterparts to be competitive.

Thank you very much.

Mr. BATEMAN. Thank you Mr. Johnsen, and all of our panel members. As I said earlier, we are appreciative and thank you for coming and sharing your views with us.

I was particularly gratified to hear you make reference to the Shipping Act and the importance of continuing the basic thrust of what is in the Shipping Act and its importance to the U.S.-flag carriers.

If any of you would care to update the panel as to whether negotiations are in progress or whether or not they appear to be likely to bear fruit, we would be glad to hear from you.

Mr. SNOW. Mr. Chairman, there are, I think, fruitful discussions underway. Chairman Shuster is well aware of those and has been kept advised. And we are hopeful that some progress can be made there.

I am personally very optimistic that there is developing a mutual understanding that will lead to some loosening of the system, without destroying the system, which will respond to the shipper's needs as they see them for some more flexibility while not putting the cart in the ditch or having the wheels come off.

Mr. BATEMAN. My perception early on was that a new group who had not previously dealt with these issues was finding the notion

of here is an opportunity to abolish a whole agency of government and to be a part of reinventing government and this was going to be a wonderful thing. Certainly, I think those on this panel and you have had some impact in that they better understand that this is not something that you can just lightly discard without it having some very significant implications.

Mr. SNOW. Mr. Chairman, on that score, I do think we have crossed that bridge. There is now a much broader understanding of the role that the Federal Maritime Commission plays in creating fair trade practices in this important maritime industry around the world, and that without the FMC or an agency playing that function, U.S. trading interests and U.S. commercial interests and U.S. maritime interests would be badly served.

Mr. BATEMAN. I am on the subcommittee which deals with that in the Transportation Infrastructure Committee. I am on the committee and I touch base on a recurring basis with my colleagues, Mr. Coble and Chairman Shuster, and will continue to do so and hope that the discussions that are ongoing, are going to produce a bill that everybody can be very pleased with and will keep intact the things which are critical to the American flag and merchant marine.

Do any of you have any specifics you would like to give us in terms of the regulatory reforms that are in the bill which you look upon as being particularly important?

Mr. VERDON. Well, the bill that is before us, in general what I would like to see and what I think the panel would like to see, is going back to the bill that was marked up last year. That is the result of a compromise amongst all the carriers. As I said, the unions and just about everybody who touches maritime promotional reform. And that sort of laid it out. This bill that is—

Mr. BATEMAN. There is no departure in this proposed legislation from that?

Mr. VERDON. Well, the proposal from the administration is a little different in that some things have to be cleared up and worked on. But along with mixed fleets, for instance, the ability to use foreign-flag vessels while you are a U.S.-flag company and the need to do that in certain circumstances so that you have the flexibility. The need to more clearly determine the eligibility of vessels for the program and to make sure that if you are not eligible—or rather you are eligible but you do not get into the program because of a lack of funds, that you have some escape mechanism, that you are not stuck in a situation where you are U.S.-flag but your competitors are receiving fees and you are not receiving anything. That would make it worse than it is today in many ways.

Those kinds of things have to be worked out. But there really is nothing from a specific standpoint that would torpedo the efforts that are going on. It really is just working it out and making sure that it works to everybody's satisfaction.

Mr. BATEMAN. Well, obviously the political environment here in Washington has undergone some significant change with the 104th Congress. Otherwise, I would not be sitting here in the middle of this bench, I can assure you.

But even in that context, I hope that this panel and through the National Security Committee that we can replicate the kind of good

work that I am very proud that the old Merchant Marine Committee was able to accomplish last session. And you cannot imagine how very disheartening it was to me to see all of that good work die without becoming law in the 103d.

Let me turn now to Mr. Taylor.

Mr. JOHNSEN. Mr. Chairman, I think on the eligibility of the vessels, the last bill as was compromised had the various types of ships that were prioritized by the DOD. The current bill would, in effect, opt out our company because in the barge carrying ships would be opted out and also some of our carriers which were also considered by the DOD on a prioritized basis, and that is why Mr. Verdon says the eligibility factor is something that we think has to be addressed again.

Mr. BATEMAN. I am sure that it is going to be addressed, Mr. Taylor.

Mr. TAYLOR. Thank you, Mr. Chairman.

If you don't mind, I would like to make an observation. First, I want to compliment my Democratic colleagues for 100 percent participation today. I am only complimenting, you know, the guys who are here.

Mr. BATEMAN. I can assure the gentleman that I am going to have some discussions with my majority colleagues.

Mr. TAYLOR. And in keeping with that, since I wanted those people who are taking their time to be here to have the first opportunity to ask questions, I will yield my time to Mr. Abercrombie of Hawaii, with your approval, Mr. Chairman.

Mr. BATEMAN. Indeed.

Mr. ABERCROMBIE. Thank you very much.

I am going to try and forgo statements because I think people who know my views when I was first on the Merchant Marine Committee and then subsequently on armed services and now the National Security Committee are aware that I see this as a matter of not maritime security but national security.

I think this is the preamble to my question, that unless we are able to get the people in the Nation to understand this is a matter of national security as opposed to some special interest pleading, which could be construed as maritime by the phrase maritime security, we are in serious trouble.

I don't think the average American has the slightest idea about what is going on today, and if they heard this testimony today would be totally confused and nonplussed to find out what it meant. It would make the bill we passed yesterday, Mr. chairman, look like something with crystal clarity compared.

Mr. HUNTER. We understood it.

Mr. ABERCROMBIE. Exactly. What I am saying, that is the kind of thing, a tax cut or are you raising taxes, those kinds of things, people can latch on to it. To say that the U.S. merchant marine is on the verge of being totally decimated and disappear is something that is incomprehensible to them.

As a result, I want to take in your overview of the testimony, and I will direct my question to you, Mr. Snow, although anybody can jump in. If you take the operating differential subsidy, we call it a subsidy, I think that is a mistake right from the beginning. And the reason I say that we get hit—let me use an analogy or parallel.

The same word is used with respect to sugar, the sugar program. It is not a subsidy. It is a loan program that does not cost the taxpayer a penny. It helps us to be able to take on competition from the world. I don't call it competition. I don't call confronting slave labor competition or having foreign governments subsidize ruling oligarchs as a subsidy—I mean, as a fair approximation that we are doing the same thing. We are not.

We do not call the salaries of military personnel in our committee here a subsidy. Those are salaries earned. I don't see why we see having American crews on U.S.-flag ships under this a payment subsidy or some kind of charitable endeavor.

Capital costs for a C-17 or an aircraft carrier, we don't see that as a subsidy, that we could build it cheaper. If we do, why are we building a carrier in Newport News? Let the Japanese or the Germans or the Greeks or somebody else build it. If that is going to be the argument and if the argument is going to be crews cost more, then why don't we do what Mad King George did and hire Hessians?

I said this in Singapore when I was getting a recitation out there about how we could maintain ships cheaper in the Far East. We could crew them and all kinds of things could be done cheaper and I said very frankly to the Navy commander, then what do we need you for? Why don't we get a cheaper commander too while we were at it? That didn't occur to anybody.

I foresee the day, Mr. Chairman, when we are going to be in the situation—and let me tell you, it will be a sorry turn of the wheel—when we make a deal with the Vietnamese for Cam Ranh Bay and the whole damn Vietnamese war and everything that was associated with it turns upside down and everybody wonders what in the hell was that all about? And that is what I see coming if we do not make an investment now.

Now, what I would want to ask, then, with all of that, is what do you specifically suggest—because I read through all of this. I would like to know specifically, Mr. Snow, what you think needs to be done to turn this into a program that is not a maritime security program but a national security program that fully funds what the carriers need to have done, what the ship builders need to have done, what the seafarers need to have done?

Mr. SNOW. Well, let me align myself first of all, if you don't mind, with your comments and their overall thrust. I know you are absolutely right. I think to talk about a subsidy for U.S. Fleets mischaracterizes and misconstrues what this is all about.

The Department of Defense wants to use and have available U.S. crews. Why? Because U.S. crews provide a higher quality, more reliable, more dependable service. They are a proven service. It is a service from people who are known to be patriotic. And that is of value. And we are in the railroad business and we are in the barge line business, and we are in all sorts of business. And often the service that we provide is tailored to meet the needs of a given shipper.

General Motors wants certain kinds of cars. Often they cost more than the standard car. General Motors doesn't complain about the fact that they have a higher quality car. They pay a higher price for that.

I think what the merchant flag fleet offers is a higher quality service to the U.S. Defense Department. It offers a service that simply is not available otherwise.

Before answering more fully, I want to align myself with those comments. I think framing it that way is the only way that causes this issue to make sense. This is national security.

Mr. ABERCROMBIE. So if this panel is to make a recommendation to the broader committee as to what it is to do and in turn be able to make a case to the transportation committee and the powers that be here in the House, I need very succinctly the recommendations that you would make to improve the bill that we are going—the fundamental bill that we are operating from.

Mr. SNOW. Assure flexibility. Assure that the ships that don't get called upon by the Department of Defense are free to be used competitively without restrictions. Minimize the restrictions that attend participating in the program. I think the funding level is awfully lean, but manageable. And I think the Department of Defense ought to have access, as was suggested by Mr. Johnson, to the entire range of vessels that are available today rather than having them circumscribed by the legislation itself.

Mr. ABERCROMBIE. If we do that, I detected in your testimony here, if I read it correctly, that you believe that this will be a step toward getting us to reflag ships as American ships, even if they are foreign-built at this stage. I am sorry we got to that stage, but that is where we are right now and we have to deal with reality.

If all of these things take place, is it your testimony and your judgment, your professional judgment that we would be taking a step toward getting back toward at least reflagging as American ships and then be able to deal with the question of getting them American built again?

Mr. SNOW. I think what you are doing here is making an important step toward preserving the U.S.-flag fleet and avoiding reflagging or going foreign-flag on the part of—

Mr. ABERCROMBIE. Then we can start from there and see what we can do?

Mr. SNOW. Would certainly create a platform for that.

Mr. BATEMAN. I think Mr. Snow is telling us that we have got to stop the hemorrhaging before we can make the patient well.

Mr. Pickett.

Mr. PICKETT. I have no questions at this time.

Mr. BATEMAN. Next in order of their appearance, Mr. Kennedy.

Mr. KENNEDY. Thank you, Mr. Chairman.

I would like to ask the panel to comment on to what extent the Department of Defense, if we are always talking about this as an important sealift capability for the Department of Defense, how much have they been involved in doing an assessment based upon the threats, predictable, their needs in the future in terms of needing the sealift capability, juxtaposed to their own in-house sealift capabilities? Are there any studies they can make available from the Department of Defense on that?

Mr. LILLIE. Mr. Kennedy, I think I can respond to that in that the original program last year was sized, as I understand it, based upon a DOD study for 52 ships. We do not have access as private

parties to that study, but I am sure that you as a Member of the panel would have that access.

Mr. KENNEDY. OK, I will work through the chairman to get that.

I just want to make a point with respect to the restrictions because in looking at this, it is clear that the biggest operating mechanism in the differential between our ability to have crews and foreign vessels is the wage base. It is labor.

So when you talk about minimizing restrictions, essentially, and allowing competition, as Representative Abercrombie was talking about, basically we are racing toward the bottom. It is how are we going to be able to work out a mechanism with labor to pay people less or have less people that we have to pay, you know, wages. Maybe you could comment on that.

Mr. JOHNSEN. I will try that, Mr. Kennedy. There are a number of regulations now that we have to contend with such as trade routes, such as various port calls, such as the number of ships you have in one area or the other. These are the major restrictions that would be eliminated by this bill.

I don't think, as I said a moment ago, I think that there will be ways that we will work with the unions to reduce costs. I don't think it is the intention of the employers to race to try to do something to be detrimental to them.

I think what Mr. Snow said is that we think this is a doable program. It is lean but it is a doable program. And basically what we all have to face, that if we are going to see the U.S.-flag on the ships, we, as Representative Abercrombie said, do we want a U.S. citizen on that ship with a satisfactory wage or do we want a foreigner with a very much lower wage. But we are not trying to, as employers, to zero in on what you just talked about.

Mr. KENNEDY. How proactive has the Federal Maritime Commission been with the Department of Commerce and our Federal Trade Representative in advancing fair labor laws on our competing countries?

I mean, I know we are having to react and work out flexible labor agreements so we can keep American flag ships. But I am asking to what extent have we been trying to get the other guys to start paying fair wages and adhere to some basic standards?

Mr. JOHNSEN. I guess you have two different approaches as to the way the historical governmental setups have been. The Federal Maritime Commission has been set up as a regulatory type of body for rates, conferences, tariffs and so forth, whereas the Department of Transportation and the Maritime Administration has been the promotive side of the industry.

I would say that from your point of view, the Maritime Administration would be the one that would be doing that. And I think there is a constant dialog, but I don't see how we can, as one part of the trading arm, try to decide what the other side of the trading arm is going to do. I think that is difficult.

Mr. KENNEDY. I agree. As a Member of Congress and as someone who is seeing this global economy coming to fruition, I am worried that unless we start putting pressure on the other countries around the world that they better start paying a fair wage and adhering to some basic standards themselves, we are just going to be, as our own minority leader said, a race to the bottom in terms of medioc-

urity and low wages. And it was the same concern that was expressed by Representative Abercrombie. I know this is just one small facet in terms of the bigger issue.

Mr. JOHNSEN. Well, individually I would say to you that one of the things that we as a company have felt is bilateralism is not a bad idea whereby we have trading partners and answering your question in that way. That there should be more bilateralism where our trading partner ought to deal with our flags.

Mr. BATEMAN. If I might at this point, we have a vote coming up. In fact, we are in the course of a vote now. I am going to ask my colleague, Duncan Hunter the chairman of the procurement committee if he feels that he would rather have his time now and leave in time for the vote or would you rather recess and come back?

Mr. HUNTER. We have 6 or 7 minutes. I would be happy to recess.

Mr. BATEMAN. The panel will recess and be back as soon as we can make the vote.

[Recess.]

Mr. BATEMAN. The panel will come to order.

The Chair recognizes the gentleman from California, and chairman of the procurement subcommittee.

Mr. HUNTER. Thank you, Mr. Chairman. And thanks, incidentally, to Rusty on the staff for kind of leading those of us who need to be up-speeded on this issue, for giving us as many good basic briefing papers as you have and trying to bring us up to speed so that we can participate in a meaningful way.

Let me throw something out. Obviously we are going to have continued deficit reduction efforts. Whatever left of these ODS programs, from what I understand of the testimony, they are going down and out.

The conclusion that you are going to hear from many leaders in the executive branch and congressional branch is everything has to go and we have to move to the foreign flag. That is the way to go. The question is, Can we salvage this program?

And let me just ask you a question here. It is going to be tough to get any money out of the Treasury over an extended period of time, but it might not be tough to get tax cuts out of the Treasury. And the reason it is not going to be tough to get tax cuts out of the Treasury for shipbuilding because for practical purposes nobody is putting any money in the Treasury from shipbuilding in this country anyway. Is that accurate?

There are not big profits being made and very few hulls are being constructed. Is that accurate?

Mr. SNOW. For the international shipbuilding business, there is still a strong, viable, though smaller than it was, inland domestic shipbuilding business.

Mr. HUNTER. But I am talking about the big stuff. Uncle Sam is not making any revenues off of shipbuilding anyway because there is not any.

Is it possible for us, if we had a Ways and Means Committee that was cooperative, to put in extremely accelerated writeoffs, maybe three-year writeoffs, 150 percent instead of 100 percent deference or elimination, 10-year hiatus in paying corporate taxes, income

taxes, any species of taxes on shipbuilding profits in this country where we could go to the congressional leadership and to the White House and say, we know you cannot give us any money but we would like you to give us a tax holiday or a tax deference or an accelerated schedule.

And so my question to you, gentlemen, is, could we recoup the American-made shipbuilding industry and attract the necessary capital to do it through a program like that? And anybody who wants to answer it.

Mr. LILLIE. I will try a crack at that, but remember we are not ship builders, we are ship operators.

Mr. HUNTER. I understand, but you folks understand the industry, and you understand the need to keep American flags on American-built ships if possible; right?

Mr. LILLIE. That is right. And my understanding has been that there has been considerable work to help create an environment where the shipbuilding industry can become competitive in the commercial world. That is going to take some time. It is going to take some investment.

Now, I don't know what their tax structure is, so whether they can use tax credits very well or not, I cannot tell you. But I can tell you that I think that the will is there among our colleagues in that industry and we want to encourage it in every way possible, as long as we keep floating.

Mr. HUNTER. I got you.

Mr. JOHNSON. I think you are also asking from the point of view of the operator and one of the point of view of the operator one has to recognize that we are dealing with foreign-flag owners who, one, pay no tax, or alternatively, have accelerated depreciation already.

So you are dealing with, from an operator's point of view and an owner's point of view, you are dealing with a competitive environment that, for instance, sailors in foreign ships pay no income taxes in most cases. So that what you have to reckon from a ship-owner's point of view, you are looking at a situation—and I think Mr. Snow made it correct and Representative Abercrombie stated—what this is is a platform that we can go forward on but I think it is a minimal platform.

Mr. HUNTER. Sailors from foreign ships don't pay taxes so they are a species of foreign worker from that country's point of view that doesn't have to pay taxes, and we have some tax adjustments with respect to Americans that are abroad. But would you recommend that?

I mean, that might be one way to help meet the diminishing of the ODS subsidy if you said American crews, since American crews are going to be a thing of the past if things keep going like they are; right?

Mr. JOHNSON. Absolutely correct.

Mr. HUNTER. If they are going to become a thing of the past and they are going to become a drag on the economy because they are going to be taking social payments from government. In Jack Kemp's terms, they are going to be unloading the wagon instead of loading the wagon.

How about a tax package that would not only give a holiday to the shipbuilders but give similar treatment and say if you are run-

ning American-flagships and you are crew on those ships, you don't pay income taxes?

Now, Uncle Sam is not going to be losing any money because they are not going to be getting any money from those folks. Would that be a good booster?

Mr. JOHNSEN. I think there was recently several studies made that show that the shipowners as a result of the taxes paid by the seamen and the shore staffs and the results of the purchasing that those companies have made, that the return to Uncle Sam is about \$1.50 for every dollar that they put out. Right now, even though there has been some cost differentials for payment to the operators, it hasn't been out of pocket ultimately from the U.S. Government.

Now, second, in respect to your question concerning would we recommend that, obviously we would have to study it. I can't say it off the top of my head. But obviously I would say in my company, this is a question that hadn't reached our panel before, but I would say it would be certainly something that ought to be studied to see if a holiday for sailors and seamen as well as it is companies that are operating, it would help.

I don't think it would eliminate this program, however, because I think that we are already—when we started talking about this, there were three areas that we thought were essential.

One was the tax problem that we need to be competitive with internationally. The elimination of restrictive regulation in parity with our crew costs.

Mr. HUNTER. Thank you very much.

Thank you, Mr. Chairman.

I would just recommend that at some point we try to engage—we work on this issue and maybe try to engage with the Ways and Means Committee to put together a tax deferral strategy that will not cost Uncle Sam any money but might keep this industry alive.

Mr. BATEMAN. Well, I thank the gentleman.

I will just comment that in my opening statement I made reference to a need for ingenuity in addressing these problems, and that is really ingenuity and we will be happy to pursue it and see how we might be able to structure something.

In that connection, reference, Mr. Johnsen, was made to some economic study of the input of the shipping industry into the national economy as opposed to, quote, "the drag on the Treasury." We would be happy if you could either give us the source of that data, or if you have it available, furnish it to the committee. It would be very helpful to us in getting our job done.

Mr. JOHNSEN. We will be delighted to do that.

This study can be provided by the Mercer Management Consulting, Inc., 33 Hayden Avenue, Lexington, MA 02173-7993

Mr. BATEMAN. The gentlelady from California, Ms. Harman.

Ms. HARMAN. Thank you, Mr. Chairman.

I have a prepared opening statement which I would like to insert in the record.

Mr. BATEMAN. It will be done.

[The prepared statement of Ms. Harman follows:]

Opening Statement of
Rep. Jane Harman

Merchant Marine Panel Hearing
April 6, 1995

Mr. Chairman:

Thank you for convening this hearing to discuss the maritime security program, a program critical to the revitalization of a US merchant marine fleet.

I join you in welcoming our witnesses and I would like to take special note of two fellow Californians representing Oakland-based American President Lines and San Francisco-based Crowley Maritime Corporation. Let me also note that Matson, a signatory to the joint industry statement, also serves the Port of Los Angeles, which I have the honor of representing.

Ms. HARMAN. Let me note a couple of things. First of all, I think the reorganization of the House in this Congress has caused some very good things to happen, one of which is the formation of this panel. I think it is high time that this committee focused specifically on these issues. And under your leadership, I know we will.

The second point is, two of these witnesses represent California-based companies. I would like to say a special welcome. And Matson, which has also signed the joint industry statement, serves the port of Los Angeles, which I happen to represent.

I think the issue of not just maritime security but national security is paramount. Mr. Abercrombie is right. And let me just make an observation and see what you think of it.

Mr. ABERCROMBIE. Could that be put in the record, Mr. Chairman?

Mr. BATEMAN. Every golden word.

Mr. ABERCROMBIE. Little triumphs, little joys.

Ms. HARMAN. I will repeat that: Mr. Abercrombie is right. One more time?

Mr. ABERCROMBIE. No, that is fine.

Ms. HARMAN. He is often right. Why is he so surprised?

But as we focused in other parts of national security, I think we have been concluding, certainly I have, that we cannot afford two separate industrial bases, a defense industrial base and a commercial industrial base. If we ever could afford that, the time is over.

And so we are looking certainly with respect to satellites and aircraft and other things at ways to collapse those bases into one. And I think we need to do that in the maritime area as well. And to the extent that we talk about maritime security, we need to look at our commercial industrial maritime base as part of that equation. We cannot ignore that.

And I just wonder what your observations are or your reactions to that statement?

Mr. SNOW. You know, in effect, Ms. Harman, this program that we talked to you about, which is really derived from Andy Card's suggestions of several years ago, is just that. It is an effort to use the private sector and national security in a way that reduces the cost of accomplishing national objectives, reduces them by relying on a low-cost, efficient competitive private sector which becomes in effect an adjunct or an arm of the DOD.

I think you are absolutely right. I think we have to be looking for low-cost ways in these days of scarce resources enormously scarce resources and budget constraints to do that, and it seems that this is in furtherance of those objectives.

Mr. LILLIE. I think particularly the spirit of Mr. Abercrombie's statement that this is not a subsidy, some years ago I testified on this and called it a service. Because it is a service that we offer. And the country can decide whether it is a good service to buy.

I think it is pretty obviously an economic service to buy from a national security point of view or it can say no. And if it says no, then we should be able to operate flexible and commercial interests move forward as individual companies.

But the main subject here is, is this a good service for our country to purchase?

Ms. HARMAN. Anyone else?

Mr. VERDON. If you take a look at what it would cost the military complex to do what we did in Desert Storm for the government and to duplicate those services, the studies show it is upwards of \$6 and \$7 billion to build a fleet that would be ready to move when it is needed. And even with that \$6 and \$7 billion, it would not be as good because there was no manpower. It would be a fleet in mothballs.

When you talk about combining the two, this is a perfect example of what we are doing. We can do for \$100 million a year what would cost \$6 to \$7 billion to almost duplicate, but not quite do it as well as we do.

And second, it should be remembered that if there is not a program we are doing to be an extinct species. There are no ands, ifs or buts, 100 million is an awful lot of money. But the question is, Is it worth it? Is this as good a buy that you can get for the dollars that you have to spend?

And if we can cut it down and get it reduced to \$100 million, then that decision has to be is it worth it. And if you look at the \$6 or \$7 billion that would cost to duplicate the fleet and look at it in terms of overall intermodal expertise that each company has to move boxes all over the world, which that \$6 or \$7 billion fleet would not know how to do, not because they couldn't learn it but because they would have never done it before, the question is pretty much self-answered. Namely, that it is a good purchase. Because if it were not here, you could not have moved the cargo in Desert Storm.

Ms. HARMAN. I totally agree with you. I think the way to articulate this is not in terms of subsidies. That is a loaded word and sounds like the old way of doing business. But this is the most effective way to leverage private sector or commercial resources for defense needs. And we get a better, faster, cheaper product this way compared to any other alternative.

Mr. VERDON. Absolutely.

Ms. HARMAN. Mr. Johnsen?

Mr. JOHNSEN. I have nothing to add. You articulated it better than I could have.

Ms. HARMAN. This is a good day for Mr. Abercrombie and me.

Let me just ask one other thing. I have been told about the Mercer Group, which I gather was asked to study the defense utility and cost-effectiveness of using U.S.-flag vessels for sealift, is this the study that we should all be looking at? Does this provide some data that this panel could learn from?

Mr. JOHNSEN. There are two studies. One is the Mercer Study, which I think was very well put together, and the other is the Nathan Study, and we will see that you get both of those.

Ms. HARMAN. Thank you very much.

I yield back, Mr. Chairman.

Mr. BATEMAN. Thank you, Ms. Harman.

We here at the center of the committee table, responsive to Mr. Abercrombie's exhortation, have now come up with operating differential adjustment or operating differential retainer. We will be brainstorming some more as to how we can get away from that obnoxious work subsidy and try to get the debate framed in a context that is more realistic.

Now, I call on the gentleman from Maine, Mr. Longley.

Mr. LONGLEY. Thank you very much, Mr. Chairman. I apologize for being here late.

And I am not sure if there was any testimony offered on this subject, but I would be very interested. There has been a lot of discussion about the role of sealift in conjunction with Desert Storm, and I wonder if each you could briefly describe your experience in terms of the posture that you companies took, how it impacted you, were you involved or to what extent.

Mr. Johnsen.

Mr. JOHNSEN. All right, I would say that we had a number of our vessels, we had, if I now remember, we have three ships that are under a charter to the Navy that were called military pre-positioning ships. Those three ships were in the Persian Gulf within 2 weeks. And we had some of our LASH vessels which were highly leveraged with ammunition and other supplies. And we were in Dammam within 7 days. We sent our staff out.

We had at one time a total of 60,000 tons of ammunition in and among our ships. And I think it was important to say that not one of our sailors made any objections about that fact, of the sort of concentration. Overall, they are civilian workers and they were involved in a very tenuous set of circumstances at the time. And we then consistently diverted some of our regular liner vessels that gave us space and diverted from our regular service, much to the upset of our shipper friends, but we did that, as did our other colleagues here, and we also carried a considerable amount on a consistent basis for supportive work, so this is what we did.

Mr. LONGLEY. Mr. Verdon.

Mr. VERDON. Crowley Maritime turned three vessels over to the military. American Condor, the American Falcon, and the American Ambassador. Ro-Ro type vessels carrying heavy equipment into the military area.

Mr. LONGLEY. Was this a voluntary initiative on our part or pursuant to an agreement?

Mr. VERDON. Ours was pursuant to a negotiated agreement with the military. All three ships I mentioned were not laid-up ships, but were actually operating with crews on them in commercial services, and it was a difficult decision on everybody's part whether to give up those ships. Because once you give them up, you are out of your commercial service. But recognizing our obligation, we gave them up to the military and pulled out of the commercial service in that area with those vessels.

The Ambassador is back working. The Condor and Falcon are still under charter to the military. But if we did not own those and they were not American-flag, and if we were chartering them in as long-term lease as a foreign-flag vessel, which is probably the way we would do it instead of owning it, we would not have been in the position to give those ships to the military.

Mr. LONGLEY. The agreement was pursuant to what program?

Mr. VERDON. Pursuant to the program, when you bid on military cargo, you agree to make ships available to the military in terms of a national emergency. But over and above that program, I think even if there were no such program, there would be no doubt that we would have worked with the Government.

You know, we the—the company is an American-flag company, with Americans, and we were in a time of national emergency, so we turned them over. I think that is one of the things that people miss in all the debate, they talk about there is an agreement or a program. Having an American-flag crew on the vessel has something that is intangible and hard to describe, but what it really is is that you will be there at the time of a national emergency. Period.

Mr. LONGLEY. Mr. Lillie?

Mr. LILLIE. Thank you for your question, Mr. Longley. American President Lines was fortunate in that this did happen in our primary operating area of Asia. Therefore, we were able to quickly move to carry the cargo that we did carry, which by the way, was 39 percent of all of the containers carried in Desert Storm to Dammam through our regular liner fleet schedule without major disruption to our commercial customers.

So we were able to adjust very rapidly. I might add that we also used extensively the double-stack train network that we operate throughout North America to gather cargo and deliver it through our terminals on the West Coast and then into our maritime system. And that, I think, is a key point here in what we are discussing today. Because the total intermodal operating capability that we bring to bear around the world as commercial operators is unexcelled anywhere in the world. There is no other place in the world that can provide intermodalism with the information systems and communications system support that we do.

And that led, in fact, to Operation Team Spirit, which was a test program in Korea, which allows for immediate, instantaneous, and 100-percent accurate, identification of where a container is in the system, using electronic tags. So I think we have had a very good experience operating in a partnership with the military on these types of issues.

Mr. LONGLEY. Mr. Snow?

Mr. SNOW. We responded much the same way. Sealand operates global service; service from the major ports of the West Coast to Asia. From the major gulf and U.S. East Coast ports to Europe, and between Europe and Asia, and Latin America and so on, with a system of global terminals, and many, many container ships and feeder ships. About 90 ships in all.

As I recall the numbers, we moved about 35,000 boxes of the 80,000 boxes, so a substantial part, just as American President did. We leased in thousands and thousands, really, of containers to augment our own container capacity so that we would have an adequate number of boxes to move the fleet. And then we moved the military requirements in accordance with our ongoing commercial business displacing, in some cases, obviously, some commercial cargoes, but trying to accommodate both. A great deal of our cargo moved through our port at Algeciras, the Rock of Gibraltar area of Spain, and was fanned out in smaller ships that could get into the Persian Gulf.

We used a few foreign-feeder lines for that service, found that the experience was not as good as we had hoped for because on some of those ships we had crews that refused to go in. We substituted total U.S. crews then and found that the usual perform-

ance of the U.S. crews—dependability, patriotic, there when you need them—proved to be the wave of the day.

So our experience was a good one, except for those few instances with foreign crews, and moving 35,000 containers on an—existing additional containers on an existing network, utilizing the information systems and the terminals that were already there. And the ships there were already moving between the major ports of Europe and Asia and the United States, which means that we are able to accommodate the needs of the military in ways that simply I don't see how they could ever replicate.

Mr. LONGLEY. Mr. Chairman, I ask unanimous consent for one other statement. I would submit this for the record as kind of an open request. I don't know whether there are any documents or studies or reports that have been compiled, experience that you have encountered, particularly the problems with foreign crews. But if we could find that for the record, I think that would be very valuable information for this committee, and I am not sure, Mr. Chairman, even if the Defense Department has that data.

Mr. BATEMAN. I am not sure in what form they have it, but this Member who has been here going into the 13th year can remember too many occasions when we have heard testimony with respect to the Vietnam war, where foreign crews would not operate in areas where our vessels or where we need to have our troops supplied. There are definitely instances in the gulf war where foreign ships and crews were unwilling to operate.

There were also, going back to the chartering of the Kuwaiti tankers during the Iran-Iraq war, foreign ships were unwilling to go into the waters of the Persian Gulf. So there are numerous instances, and we will see if we cannot have staff launch an effort to compile some of that information.

Mr. LONGLEY. Thank you, Mr. Chairman.

Mr. BATEMAN. At this point, I would like to recognize the gentleman from Mississippi, Mr. Taylor.

Mr. TAYLOR. Thank you, Mr. Chairman.

I will open this up to the panel.

The first question is. Do you consider each of your vessels a separate cost center? And if the answer to that is yes, then what percentage of the total—and I do mean total cost of operation of that vessel—is the actual purchase cost of the vessel or the monthly note that you have to pay toward the acquisition of that vessel? If there are any industry standards on that?

Mr. JOHNSEN. Well, I will try to—you want somebody to try to answer that particular question?

Mr. TAYLOR. I would, please. That is why I asked it.

Mr. JOHNSEN. I will be happy and see if we cannot give you some insight into it. Obviously, the first thing is the capital cost of the vessel, whether it is \$20 million, \$30 million, \$40 million, \$50 million, you have to apply that.

Assuming that you were to take a new building in the \$60 million range, one would—I would say that probably you are looking at, from a cost point of view, probably in the neighborhood of about—for capital costs, probably about over 100 percent over your operating costs. In other words, your operating costs on a daily

basis, what you are doing today, your capital costs would be about twice.

Mr. TAYLOR. Twice the amount?

Mr. JOHNSEN. Yes.

Mr. TAYLOR. So if your total budget is \$3, two of those goes to acquisition.

I want to compliment my colleague in Hawaii for some comments that he made earlier in the day. I thought he made a brilliant observation. He said, you know, if this committee were to recommend to the Air Force that they try to solve our ballistic missile defense problem by going to Toshiba or Sony, the Air Force generals would go berserk. And if we recommended the acquisition of a foreign product to solve our problem, the agency responsible for that would again go berserk, and for good reason.

And the only time they change their tune, and when it comes to ships, as unfortunately the Marines did just recently in the purchase of three foreign-built roll-on-roll-off ships for their preposition ships. They say we are going to fix them in America, but they still bought them foreign.

And I do realize now that you have told me a tremendous part of your cost is the acquisition. And I think the solution to what I want to do and what you want to do is somehow we have to keep your companies in business, but I think we have to have American ships to do it.

One of the solutions that I was not aware of that someone from the private sector, a small shipyard owner from Burlington, Mississippi, pointed out, he made me award of the title XI program, and this committee was good enough not only to renew, but make it a little bit bigger. A low-cost way of getting some ships built here.

What else would we do, without breking the Treasury any worse? What other low-cost alternatives are there out there that you gentlemen are experts on that this Nation could be doing to try to solve your problem, which is to compete in a very tight foreign market, but also solve this committee's problem, which is to ensure that we have a national shipbuilding base that we can call on, not only today, but 10 or 20 to 30 years from now?

Mr. JOHNSEN. As Mr. Lillie said, we are not shipbuilders and, therefore, I don't see that we can answer. I think they can answer how they can be competitive.

All we are saying is to keep the cost down from an owner's point of view, one has to say that we should be allowed to get our equipment at an international price. There are a number of shipyards that have stated, and I have talked to some of the CEO's of those shipyards, that say they feel they can be competitive internationally. There are others who say they cannot.

Our viewpoint is that we are very supportive of that sort of industry and we think they ought to be there. But you cannot let both of us go out of business because we are trying to some way tie an anchor to one or the other.

I think you have to say to us, we are going to make you as owners and operators competitive, and we are going to deal in a very competitive way, and we are going to see what we can do to help them, perhaps a tax holiday, perhaps some of these other things,

because, frankly, we think that they should be favorably considered.

We have had the benefit of building ships, as I said earlier in Avondale. They have been very efficient ships. They are still working for us in good state of repair. But there is no way that we can sit here because we do not know their activities or what they do to build the ships. That is something that you would have to talk to them about.

Mr. LILLIE. If I could add a little bit to that, please, Mr. Taylor. I think that just as a businessman observing this from maybe a little bit of a distance, but not too far, that it is important that the shipbuilders recognize that they are going into, in effect, a new market, because they have been out of the commercial shipbuilding market for some time now in terms of the total scope of that market, and focus their efforts on a few places where they can be very good. And in turn, I think our Government can help them with the start-up costs of that focus. And I know that there has been some specific legislation to provide that kind of support.

But the startup in some of these areas is not immaterial. And if we could get very good at a few things, then we can start to broaden ourselves into a much more significant role in world shipbuilding.

Mr. SNOW. Our vessel costs are—that depends what vessels and what strings, and so on—are basically operating costs on the vessel are 20 to 30 percent of the total cost, operating costs. So the vessel costs are an important part of our total cost.

And we do look at vessels as, in effect, profit centers in the sense that if you have got a string of vessels in this trade, just take a trade, take Asia to Europe, and the return on those vessels is lower than the return that some of those vessels would secure in alternative trades, then some number of those vessels will be redeployed. And we are constantly redeploying some portion of the fleet from lower return to higher return trades. That is just what you do in any line of business, redeploy your assets.

In terms of what can be done for the shipbuilding business, again, I don't hold myself out as any expert on that. But one thing that ought to be considered is removing some of the current regulations that cause ships built in U.S. yards to U.S. regulatory specifications to be about 6 or 7 percent higher than the cost of those ships built to international standards. It is a real detriment to disincentive to building U.S.-flag ships, the ships in U.S. yards.

We recently had some experience with that and built five new container ships, and we talked to the U.S. yards. If they are built in the U.S. yards, they are built to the U.S. standards. That added very significantly to the cost of these very expensive vessels. And was a factor, frankly, in our going foreign flag.

Mr. TAYLOR. If I may for the record, Mr. Chairman, request that the panel—in your statement you say that certain regulatory changes are needed to make it more cost-effective, but you did not mention any specifics. I am asking for the record if you would provide those specifics?

Mr. SNOW. Sure.

[The information referred to was not provided for the record.]

Mr. BATEMAN. Thank you, Mr. Taylor.

I might say in that connection that there is some ongoing discussion with reference to the specifics, and we will certainly be following up because we want your input to try and make this the best bill we can make it.

With that, and since we have to go to the floor to vote on the conference report on the Paper Reduction Act, I am going to ask if our panel would be excused with our very deep gratitude for your being here today, and if the second panel would take their positions, we will return as quickly as we can vote.

Thank you very much.

[Recess.]

Mr. BATEMAN. I apologize to our second panel that things have run a little longer than perhaps they might have, but, obviously, we look upon our proceedings today as being very, very important. And certainly the second panel is extremely important part of the equation that we seek to deal with.

The second panel, I will introduce all of you, and we are indeed delighted to have you.

We have Mr. Michael Sacco, President of the Seafarers International Union; Mr. Charles Crangle, Executive Director Congressional Legislative Affairs for American Maritime Officers; James Hopkins/Secretary, Treasury of International Organization of Master's Mates and Pilots; Mr. Joel E. Bem, President, Marine Engineers's Beneficial Association; and Tal Simpkins, Director of Legislative Affairs, District No. 4, National Maritime Union, Maritime Engineers Beneficial Association.

Gentlemen we are happy to have you.

My understanding is that Mr. Sacco is the duly designated lead-off hitter, and then we will be happy to have comments from all the members of the panel.

STATEMENT OF MICHAEL SACCO, PRESIDENT, SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA

Mr. SACCO. Thank you, Mr. Chairman.

My name is Michael Sacco, President of the Seafarers International Union of North America, and this statement is presented on behalf of the American Maritime Officers, represented here by Charlie Crangle; the International Organization of Master, Mates and Pilots, represented by James Hopkins; Marine Engineers' Beneficial Association, represented by Joel Bem; and the National Maritime Union, represented by Tal Simpkins.

Together, Mr. Chairman, our unions represent the more than 50,000 men and women who comprise America's licensed and unlicensed seagoing work force.

At the outset, we wish to convey our deep appreciation to you, Mr. Chairman, for your efforts in support of the U.S.-flag Merchant Marine and the enactment of much-needed and long-overdue maritime revitalization. The passage of maritime reform legislation by an overwhelming majority in the House of Representatives in the last Congress demonstrated a clear recognition that our Nation must put in place the framework to rebuild our fleet, preserve and create American jobs and to make our industry more competitive, economical and efficient.

Enactment of maritime reform legislation is essential to our Nation; our country's security, the survival of our industry and the thousands of American jobs that are at stake.

The question is whether the United States, since the leading maritime power, will have a Merchant Marine. The decision will be made by the Congress this year. It is a decision where delay now translates into lost ships and lost jobs.

Already a number of military-useful vessels have received permission from the Government to reflag foreign.

We strongly disapprove of these foreign reflaggings. And the fact that every single one of them has not been conditioned on a firm commitment to the U.S. flag when maritime reform is enacted. To prevent further reflaggings, we must enact a new maritime program this year.

Mr. Chairman, the unions sitting at this table fought hard for the passage of legislation in the last Congress and pledge to continue to fight until the Congress passes and the President signs into law a maritime program that will ensure an active American-flag Merchant Marine in the years to come. You have our pledge on that, Mr. Chairman.

As Congress debates the future of the U.S.-flag Merchant Marine, there are a number of points we believe are key to its deliberation. First, only a U.S.-flag, U.S.-citizen crewed merchant fleet provides our country with the guaranteed availability during time of war or national emergency.

There is no such thing as an effective control fleet. Without American crews, without firm operational control under American laws, effective control is merely a front to allow vessels to avoid American taxes, regulations and operational requirements while enjoying all the benefits of participating in our open and profitable shipping trades. American crews are the only mariners who respond without hesitation or regard to personal safety, as you have heard here today, as they have on every occasion in the past, to each and every call to arms from our Government.

The issue of crew reliability is crucial. During the Persian Gulf war, Japanese sailors refused to sail their vessel into the Persian Gulf and to carry weapons and ammunitions for the allied effort. And we were defending their oil with the whole world on our side.

What happens in the future when international support is not so broad or the issue not so clearly drawn? All the vessels in the world, all the documents of effective control drawn up at peacetime are worthless if the crews will not sail the ships into harm's way as called for by the U.S. Government. American crews loyal to the American flag are the only true guarantee that the Nation's interests will not be jeopardized.

The second point we would like to emphasize is that the enactment of maritime reform legislation will not simply maintain business as usual for our industry, H.R. 1350, the Clinton administration's maritime reform proposal, represents deregulation and regulatory reform for those participating in the new Maritime Security Fleet program. Working under fewer regulations, American operations will be able to compete more effectively.

In this regard, we understand the desire on the part of American vessel operators to have greater flexibility and freedom to remove

vessels from the American flag. However, we remain convinced that maritime reform legislation should first and foremost encourage a U.S.-flag fleet, not a foreign-flag fleet.

We believe that only limited exceptions to existing procedures required before a vessel is reflagged should be adopted. To grant an operator blanket authority to remove from the American-flag vessels which are eligible for the Maritime Security Fleet, and for which program funds are available is contrary to the best interest of our Nation and the goals and objectives of this legislation to promote a U.S.-flag maritime industry.

Finally, we want to stress that debate over maritime reform legislation is also a debate over the necessity of our country to participate in the carriage of our exports and import trade. Allowing foreign vessels to gain total control over our trade, especially as the United States moves to eliminate international barriers, would create an opportunity for economic blackmail.

The United States can only realize the goals of free trade if it remains a full participant in all aspects of international trade, including shipping.

In conclusion, Mr. Chairman, we strongly affirm our support for the enactment of maritime revitalization legislation which fosters the growth of a newer, more modern, efficient fleet of U.S.-flag vessels crewed by U.S. citizens. We assure you of our commitment to work with you to enact maritime revitalization legislation this year.

Thank you, Mr. Chairman.

And if anyone else on the panel has any additional comments they would like to make——

[The prepared statement of Mr. Sacco follows:]

STATEMENT OF THE

AMERICAN MARITIME OFFICERS

INTERNATIONAL ORGANIZATION OF MASTERS, MATES & PILOTS

MARINE ENGINEERS' BENEFICIAL ASSOCIATION

NATIONAL MARITIME UNION

SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA

TO THE

SPECIAL OVERSIGHT PANEL ON THE MERCHANT MARINE

COMMITTEE ON NATIONAL SECURITY

APRIL 6, 1995

Mr. Chairman and Members of the Panel:

This statement is presented on behalf of the American Maritime Officers; the International Organization of Masters, Mates & Pilots; the Marine Engineers' Beneficial Association; the National Maritime Union; and the Seafarers International Union of North America. Together, we represent the more than 50,000 men and women who comprise America's licensed and unlicensed seagoing workforce.

At the outset, we wish to convey our deep appreciation to you, Mr. Chairman, for your persistent efforts in support of the United States-flag merchant marine and the enactment of much-needed and long-overdue maritime revitalization legislation. The passage in November, 1993, and August, 1994 of maritime revitalization legislation by an overwhelming bipartisan majority in the House of Representatives was due to your efforts and those of many of your colleagues on this Panel as well as to the bipartisan leadership of the former Committee on Merchant Marine and Fisheries. It demonstrated a clear recognition that our nation must put in place the statutory and regulatory framework to rebuild our fleet, preserve and create American jobs and to make our industry more competitive, economical and efficient.

Your decision, Mr. Chairman, to schedule this hearing early in the 104th Congress, and the introduction by request of the Administration's proposed "Maritime Security Act of 1995" by you, Chairman Spence and Congressman Dellums not only provide the impetus to restart the process but demonstrate conclusively that the need to enact bipartisan maritime revitalization legislation this year is greater than ever. We, of course, remain totally committed to this effort.

In this effort we have the support of the President of the United States, as we had the support of President George Bush in 1992. This commitment is vital. The commitment of the President of the United States to a strong American merchant marine is an essential ingredient to

the enactment of any forward-looking maritime legislation. This was the case, for example, in the enactment of both the Merchant Marine Act of 1936 and the Merchant Marine Act of 1970, statutes which have long served as the underpinning of the oceangoing United States-flag commercial fleet. In the absence of the active efforts of Presidents Franklin Roosevelt and Richard Nixon, it is doubtful that these measures would have been enacted into law.

The programs embodied in these Acts have served our industry and our nation well, but virtually no program or policy is so flexible and elastic that it can function without change in the rapidly and constantly changing world of international shipping. We believe that we have the opportunity to enact legislation this year which will help the United States-flag fleet become more competitive in the global commercial shipping trade in the decade to come. Legislation can and should be enacted which addresses the realities of today's international shipping environment just as the Operating Differential Subsidy program and its related regulations helped our fleet function in a time when our country set the standard for the rest of the world's shipping.

It is impossible to overemphasize the importance of enacting maritime revitalization legislation this year. Our country's security, the survival of our industry, and thousands of American jobs are at stake. Last week, Maritime Administrator Admiral Albert Herberger stated, "without a maritime reform bill . . . for the first time in modern American history, our U.S.-flag presence in international trade will vanish, along with our civilian sealift support, seafaring jobs, and the technological leadership of our American carriers." The question then is whether the United States of America, once the world's leading maritime power, will or will not have a merchant marine. This decision will be made by the Congress of the United States this year.

It is a decision where delay now translates into lost ships and lost jobs. Already, in just a few months, a significant number of vessels, including militarily useful vessels, that would have been flying the U.S.-flag have received permission to go foreign. We strongly deplore these foreign flaggings -- and the fact that every single one of them has not been conditioned on a firm commitment to the U.S.-flag if maritime reform is enacted. But we are realistic -- and everyone in this room should be as well -- that unless a new maritime program is made law this year, reflaggings will become a flood and the U.S.-flag will fast disappear from the sealanes of the world. For our industry, Mr. Chairman, there is no tomorrow without a maritime reform program. It is that stark -- and it is that urgent.

As Congress proceeds with its consideration of maritime revitalization legislation and debates the future of the United States-flag merchant marine, there are a number of points we believe are key to its deliberation.

First and foremost, only a U.S.-flag , U.S. citizen-crewed merchant fleet provides our country with guaranteed availability during time of war or national emergency. It is the only responsible solution for economic and military security. Effective control schemes are, by contrast, a sham. Simply put, there is no such thing as an effective controlled fleet. Without American crews, without firm operational control under American laws, "effective control" is nothing more than a fiction created to give a veneer of legitimacy to vessels which avoid American tax, regulatory, and operational requirements while enjoying all the benefits of participating in our open and lucrative shipping trades. Therefore, no maritime revitalization proposal should give totally unwarranted status to a so-called effective United States controlled fleet.

The United States, the world's only superpower, should not predicate its security or the safety of its allies on anything less than the real and absolute control derived through a United States-flag merchant marine. Ours is the only fleet under the legal requisition authority of the United States. American crews are the only mariners who will respond without hesitation or regard to personal safety, as they have on every occasion in the past, to each and every call-to-arms from our government.

The issue of crew reliability is critical. During the Persian Gulf War, Japanese sailors refused to sail their vessels into the Persian Gulf and to carry weapons and ammunition for the allied effort. And we were defending their oil with the whole world on our side! What happens in the future when international support is not so broad or the issue no so clearly drawn? Do we want to risk this kind of uncertainty and delay in the future? All the vessels in the world, all the documents of effective control drawn up in peacetime, notarized a thousand times over, are worthless if the crews will not sail the ships into harm's way as called for by the United States government.

In June, 1992, General Colin L. Powell, told the graduating class at the United States Merchant Marine Academy, that:

"Since I became Chairman of the Joint Chiefs of Staff, I have come to appreciate firsthand why our merchant marine has long been called the fourth arm of defense . . .

"The war in the Persian Gulf is over, but the merchant marine's contribution to our nation continues. In war, merchant seamen have long served with valor and distinction by carrying critical supplies and equipment to our troops in far away lands. In peacetime, the merchant marine has another vital role -- contributing to our economic security by linking us to our trading partners around the world and providing the foundation for our ocean commerce.

"We are a maritime nation. Our strategy demands that we have access to foreign markets, to energy, to mineral resources and to the oceans. We must be able to project power across the seas. This means that not only do we need a strong navy, but a strong maritime industry as well. For, as the brilliant naval strategist Alfred Thayer Mahan once wrote, 'Seapower in the broad sense . . . includes not only the military strength afloat that rules the sea or any part of it by force of arms, but also the peaceful commerce and shipping from which alone a military fleet naturally and healthfully springs, and on which it securely rests.'"

Congress has the opportunity to act in response to General Powell's call for a strong merchant marine, a call also sounded by President Ronald Reagan in 1984 who affirmed his Administration's commitment "to foster and maintain the United States-flag merchant marine required by this great Nation for our national security"; by President George Bush who, in 1988, stated his Administration is "in strong agreement with the need to maintain a strong and vital domestic maritime industry and employment base . . . in the interest of national security"; and by President Bill Clinton who reiterated his Administration's acknowledgement of the important contributions made by our industry through the transmittal of proposed legislation on March 10, 1995, intended to "guarantee the existence of a fleet of privately-owned, U.S.-flag merchant ships crewed by skilled American civilian seafarers [which] ensures that U.S.-flag ships and American crews will remain available to meet national security requirements . . ."

The failure to enact maritime revitalization legislation will entrust our future security to the fiction of effective control. It will mean that American servicemen will someday find themselves dependent on the whims of foreign mariners to deliver ammunition, rations and equipment to wherever they may be stationed for whatever reason throughout the world. It is a risk our country has not yet been willing to take. By enacting maritime revitalization legislation,

the 104th Congress has the opportunity to ensure that American lives will not be placed at risk through a dangerous reliance on foreign ships and foreign crews for America's security needs.

The second major point we would like to emphasize is that the enactment of maritime revitalization legislation will not simply perpetuate business-as-usual for our industry. Rather, the legislation put forward by the Administration as well as the proposal pending at the end of the 103rd Congress represent far-reaching and unprecedented deregulation and regulatory reform for those participating in the new maritime security fleet program. In fact, many longstanding but outdated bureaucratic constraints to a more economical United States-flag merchant marine will be eliminated through this legislation. For example, for the first time, United States-flag vessels would be able to respond immediately to everchanging international trade patterns. Our fleet would be able to compete against foreign-flag vessels for cargo without the extra burden and expense of a time-consuming regulatory proceeding, a step foreign vessels do not have to take. Similarly, maritime revitalization legislation should give American operators the authority to replace older ships with newer, more modern and efficient vessels for operation under the United States-flag.

In this regard, while we can appreciate the desire on the part of American vessel operators to have greater flexibility and freedom to remove vessels from the American flag, we remain convinced that maritime revitalization legislation should first and foremost encourage a United States-flag, not a foreign-flag fleet. Consequently, we believe that only limited exceptions to the existing procedures required before a vessel is reflagged should be adopted. We believe any provision which grants an operator blanket authority to remove from the American flag vessels

which are eligible for the maritime security fleet and for which program funds are available is contrary to the best interests of our nation, and the goals and objectives of this legislation.

Finally, and of particular importance, the maritime revitalization proposal as submitted by the Administration will not increase Federal assistance to this segment of our industry. Rather, the enactment of legislation with a funding proposal as set out by the Administration will reduce total operating assistance to American vessels from a \$225 million annual program to a \$100 million annual program. Consequently, Federal support for the liner segment of the United States-flag merchant marine will be reduced by more than 50 percent.

It is important to understand that this level of support is necessary to maintain a viable fleet of United States-flag, United States citizen crewed vessels. Simply put, the industry, despite the best efforts of vessel operators and maritime labor, cannot succeed without the limited support of the Federal government to offset the multitude of vessel operation and tax requirements applicable only to United States-flag ships. There is a cost of doing business under the United States-flag that is imposed on American vessels by our government. Such regulatory and statutory requirements imposed only on American ships, regardless of their justification and necessity, add to the cost of American ships and impede our ability to compete with foreign flag, foreign crewed ships. The support level envisioned in the maritime revitalization legislation will help narrow this competitive gap.

In this connection, it is important to stress two points. First, the new maritime reform program is actually a bargain for the U.S. Government. Under it, our country will have complete access not only to a fleet of modern, militarily-useful vessels, but it will also have access to vast commercial intermodal networks which are what modern transportation and logistics are all

about. These networks will be integrated into military planning ahead of time; they will be American; and they will be ready to go because they are in use all the time. They will not have to be jerry-built when the balloon goes up. And best of all, the use of this civilian, commercial system -- that exists today -- will save the Defense Department and Federal government from enormous new expenditures on vessels and intermodal facilities which it would have to make if the commercial capability is not there at the ready.

Over the last decade as the American merchant fleet has diminished, the United States has spent billions of dollars to develop a reserve fleet of militarily useful vessels capable of complementing and at times replacing the capabilities of the U.S.-flag merchant fleet. Millions of dollars more are spent each year to maintain this fleet in a state of readiness. If the Congress fails to enact the maritime security program this year, the nation will pay a much higher price as even more reserve vessels will be required to meet defense needs. And, without a U.S.-flag fleet, who will be available to man these reserve vessels? The maritime security program is a small investment in the nation's economic and military security in contrast to the expenditures that will be required if the nation is forced to rely solely on a reserve fleet to sustain military requirements in the years to come.

Our second point -- and this is often overlooked in debates about spending for our industry's future -- is that our industry contributes to the American economy. It puts money back into the U.S. Treasury; it provides American jobs; and it generates foreign exchange. Thus, economically, in terms of federal dollars, our industry is a good investment for our nation. In terms of security, it is an essential investment.

Before closing, we also want to stress that just as the debate over maritime revitalization legislation is a debate over the security of our nation, it is also a debate over the necessity for our country to participate in the carriage of our export and import trade. Allowing foreign vessels to gain total control over the carriage of our trade, especially as the United States moves to eliminate international trade barriers, would create an unprecedented opportunity for economic blackmail against our consumers, producers and manufacturers. The United States can only realize the goals of free trade if it remains a full participant in all aspects of international trade, including shipping.

The maritime industry is dependent upon the carriage of international trade for its survival. It is not in our interest nor the interest of the United States to advocate and support legislation which would decrease the sale of American goods and commodities abroad, or decrease the number of vessels and amount of cargo handled by American ports. The enactment of maritime revitalization legislation will simply give American vessel operators exactly what our foreign competitors do not want, namely a greater opportunity for the United States-flag merchant marine to compete for the carriage of foreign trade on terms more equal to those of our competitors.

In conclusion. Mr. Chairman, we strongly affirm our support for the enactment of maritime revitalization legislation which fosters the growth of a newer, more modern and efficient fleet of United States-flag vessels crewed by United States citizens. We support the funding proposal contained in the Administration's proposed "Maritime Security Act of 1995". We remain convinced the expenditure of such funds to support the merchant marine will enhance

the economic, political and military security of our nation and do so at significantly less cost than if the government owned, maintained and operated these sealift resources itself.

We again wish to express our deep appreciation to you, Mr. Chairman and your Panel and staff for scheduling this hearing so soon after the transmittal of the Administration's maritime policy initiative. We assure you of our commitment to work with you to enact maritime revitalization legislation this year.

Mr. BATEMAN. We would be happy to hear from any of you, Mr. Bem, and then proceeding across the table, if you have any additional observations you would like to make?

STATEMENT OF JOEL E. BEM, PRESIDENT, MARINE ENGINEERS' BENEFICIAL ASSOCIATION

Mr. BEM. Thank you, Mr. Chairman and members of the panel. I agree with Mike, 100 percent of his statement. I think it pretty much summarizes our position in this matter.

We were here a year ago. We had a maritime program that close. And now we are back. I think we have a maritime program that close again. And I think it is somewhat of an improvement in the funding mechanism. I would urge the panel to support it in its totality, and let's get it done this year, whereas we didn't last year.

Just a couple of things that I would like to state from my personal experiences. I have not always been a labor union official. I was a chief engineer in 1990.

My last ship was the Sealand Atlantic, one of the largest container ships in the world. The last voyage I made on the Sealand Atlantic we took, among our general cargo, about 1,700 containers we took a full deck load of military vehicles to Algeciras for transshipment to the Persian Gulf.

That part of the leg went well. We delivered the military vehicles to Algeciras on time. They were offloaded and we continued on our way to northern Europe.

That particular cargo, as it was reported in the Journal of Commerce, was delayed because the feeder vessels would not take it—the crews would not take the cargo on to the Persian Gulf, alternate vessels had to be procured to do that.

What is interesting about this whole story is the particular feeder vessel was a former Sealand U.S.-flag vessel. Because of the economic policies in place, Sealand had to reflag those particular vehicles.

They were flagged to another Asia company, crewed with foreign crews, and that cargo stayed in Algeciras longer than it should have. I can assure the panel that had we been directed to take the cargo on to a beachhead in Basra, Sealand Atlantic would have done it. The foreign-flag vessel did not. And I think that is the one thing that we have to be focused on. We need a sealift capability for this country now and we need it in the future. And I think this type of program is a good start to get that type of capability.

Mr. BATEMAN. Thank you.

Mr. Crangle, anything to add?

STATEMENT OF CHARLES CRANGLE, EXECUTIVE DIRECTOR, CONGRESSIONAL AND LEGISLATIVE AFFAIRS, AMERICAN MARITIME OFFICERS

Mr. CRANGLE. Thank you, Mr. Chairman.

Mr. Sacco has adequately represented the views of the American Maritime Officers with regard to this bill, H.R. 1350. Apropos of the previous panel, we do have 20 or so clippings from the war, starting with the Jack Anderson column early in the war when the one ship refused to carry goods out of India, and we would be happy to bring those for the subcommittee and enter them in the

record. We stand ready to answer questions, but Mr. Sacco has adequately represented where we stand.

[These documents can be obtained from American Maritime Officers. It was provided to the National Security Committee and is held in archive.]

Mr. SIMPKINS. Mr. Chairman, we want to add our thanks to you and the panel for your efforts on our behalf.

Thank you.

Mr. BATEMAN. Thank you, Mr. Simpkins.

Mr. Hopkins?

Mr. HOPKINS. Yes, sir, Mr. Chairman.

In my career going to sea, I have gone from cadet to captain of a merchant ship, and I have seen many years, many distinguished people trying to save the American merchant marine. I think a lot of people have tried, and it is sort of like a lot of people have rung the fire alarm but no one has brought along the fire hose. And I certainly hope that now somebody comes along with the fire extinguisher or fire hose to help us in our hour of need.

Thank you.

Mr. BATEMAN. Thank you, Mr. Hopkins. And thank all of you.

Let me comment to you before I turn to my colleague from Rhode Island, Mr. Kennedy. That I appreciate the fervent and eloquent statement that has been made on behalf of Maritime Security Act or initiatives. I am particularly impressed with the testimony that refreshed my recollection of the Gulf War and that very unusual phenomenon, and the emphasis that you rightfully put upon it, that here was the broadest-base international coalition ever brought to bear in a conflict, and yet, we could not get many ships with foreign crews that would operate, even on behalf of that broad a base, a coalition, and even when it served their interests to have been participating. It is a powerful commentary on why having American-crewed merchant vessels is a vital part of our national security.

Mr. Kennedy, do you have some questions?

Mr. KENNEDY. Thank you, Mr. Chairman.

I would like to ask Mr. Sacco to comment, if he would, on the substandard wages that the other flag ships, what the experience is from your people that have you heard from just what is happening on these ships. And also if you could comment on the substandard operating practices of some of these foreign-flag ships as compared to our own U.S.-flag ships.

Mr. SACCO. Well, when you talk about competing in the international arena, there are all different types of competition. You have the runaway flag operator, which seems to be the operator undercutting everybody. The wages there can run from \$400 a month, whatever they can get the crews for, and the last edition of our newspaper we have photos of a bulker that docked in Canada. A Cyprus ship that is only 10 years old.

If you look at that ship, it looks like it is 50 years old, The crews on there were making \$300 a month. When you take a look at the living conditions, they actually had oil drums inside a man's room. No toilet. We got these pictures, they are in our paper. No toilet. Down in the engine room over a manifold, there was a hole in it.

They cut a 45-gallon drum in half. Put it up and welded it on. We have got pictures of this.

The standards and the conditions are a joke. The people who approve the inspections of these vessels have to be in the owner's pocket because that ship would never leave an American port, I could tell you.

The standards are very bad. The pay is bad. The food is bad. I mean, we got a poor crew right now as I speak, in Virginia in Norfolk, VA, the poor Filipinos have been here 9 months. We have been spoon-feeding these guys. The ship still has not been sold. They are living in a hotel that was just bought by somebody else and they are going to throw these poor guys out on the street. They have been living here 9 months and they cannot find the owners of the Greek shipping company. And we have been feeding these guys and so have the people in the churches.

This is what—the third flag is really the most horrible sight you ever want to see in terms of crew, wages, standards, and conditions. And if you get a chance, Congressman Kennedy, and get a copy of our paper, I would like for you to actually see these were pictures that were taken by an ITF inspector when he went aboard it, it is unbelievable.

Mr. KENNEDY. I would like that if you could submit it to me and maybe to other members of the committee.

What is the Organization for Economic Cooperation Development doing about putting some pressure—I mean, if we are a big trading partner of these other developed countries, why are we, as Mr. Johnsen said earlier, doing more to have a bilaterally agreement with our trading partners, saying if you are going to ship with this country, we are a big consumer, why are you not going to adhere to some basic standards?

Mr. SACCO. I don't think they consider that when they bid for the cargo. They don't take that into consideration at all.

Mr. KENNEDY. May you could provide for me some ways in which you see this being remedied. I don't know through inspection processes, through international trade agreements. Maybe you could supply me some opportunities to pursue that.

Mr. SACCO. I will.

Mr. KENNEDY. And I would like to ask Mr. Hopkins what is he sees as the impacts of these agreements going forward on the Merchant Marine academies, given that is within this committee's jurisdiction and particularly the subject of this current legislation?

Mr. HOPKINS. Yes, sir, I graduated from Kings Point in 1959, and I can tell you it is very difficult for 4 years, an arduous school, but the complexity of ships today, when I first started, we were using magnetic compasses, and now we are using satellite technology. The use of a sextant has basically disappeared as long as the electronics are working. And all the educational institutions, the ones that the unions have, we have simulators 30 miles from here that we have to keep up with the technology as it changes.

I think the Merchant Marine Academy at Kings Point and the other academies that are helped by the Government, provide not only merchant mariners in time of need or national emergency, but they do contribute to other economies. There are many Naval offi-

cers, admirals that are part—from many action. So we play an integral part in maritime education.

As we know, we have to maintain our standards so that we can be through this the most competitive in the world, and we believe that are the best at our trade.

Mr. KENNEDY. May I add, Mr. Chairman, given the testimony earlier that the merchant marine provides a reserve pool for our military in a time of need that, maybe you could comment upon the impact of the demise of the merchant marine with respect to the demise of that reserve pool of service people that could help us in those times of national security risk.

Mr. HOPKINS. As the ships disappear, so do the people who man the ships disappear. And we have all seen in this business it is feast or famine for a merchant sailor, and if there is a war, everybody wants you. You are in demand, you can go and you can sail any place.

But during the other times when there doesn't seem to be any national emergency, I have been unable to train my wife not to eat while the national emergencies are not on hand. I have to provide food and lodging and everything. And of course, I have chosen my career to be a sailor to earn my living, and I am very happy with my career. And if this was not available to me, I would have to go and choose another career.

And when you get too many of us going and choosing other careers, and then God forbid, that some national emergency does come up, where are we to come back and man the ships that some of our citizens, or in foxholes, I think they would like to see an American sailor bringing the ammunitions and the security of that.

I know Vietnam was one area where I was engaged in. And it was from the time we were observers until the time we left. I think people appreciated the ammunition that was there when they needed to reload. We had it there. We had all the materials that were necessary to maintain an armed conflict, and we can carry it. And I believe that your only security is the American citizen sailing on American-flag ships.

Mr. KENNEDY. Thank you very much.

Mr. BATEMAN. We now have another vote apparently, but we can begin and continue for about 5 minutes.

Mr. Abercrombie, and then we will come back as quickly as we vote.

Mr. ABERCROMBIE. Thank you very much, Mr. Chairman.

Mr. Sacco, and perhaps, Mr. Crangle, you could answer this, and any of the others, if you have had some connection with it.

One of the things that has been brought up, and I hope that maybe some representatives of Mr. Snow and the American President, and so on, are still in the room, because I wanted to ask them the same question. Have you had any contact and to what extent and degree have you had any contact with the U.S. Trade Representative, Mr. Kantor and his office?

Mr. SACCO. None, that I know of.

Mr. CRANGLE. To the best of our knowledge, we have not had an official relationship with Mr. Kantor at all.

Mr. ABERCROMBIE. When someone brings up this so-called trade agreement that we have that precludes—says, preclude the enact-

ment of any new assistance programs in the maritime industry, our U.S. Trade Representatives has not had word one with you about what the nature of that agreement may be?

Mr. SACCO. Not to my knowledge.

Mr. CRANGLE. You are talking about this OAC?

Mr. ABERCROMBIE. I am.

Mr. CRANGLE. No, sir, we have had no contact with Mr. Kantor that I am aware of.

Mr. ABERCROMBIE. Do you know, even if by hearsay, whether some of the companies like American President or Crowley or Central Gulf, and so on, have had any kind of extensive discussions? I see some heads nodding in the room.

Mr. Chairman, I find it extremely interesting that the Trade Representative doesn't get together with the people who are going to be affected on these ships. Do you think there is free trade now on an equal basis, level playing field?

Mr. SACCO. Never.

Mr. ABERCROMBIE. My judgment of your statement is that it is the exact opposite.

Mr. SACCO. Yes, it is.

Mr. ABERCROMBIE. Following up on Mr. Kennedy's question, then, let me just preface this quickly, I don't think that I am bound by any agreement. I never voted on anything. This is not a treaty. It is not something that has gone through the U.S. Senate, let alone anything else.

I don't think, Mr. Chairman, that we are bound by a damn thing about this OACD. I am a Representative in the U.S. Congress, and I don't know where the Greek shipping owner is that you are talking about.

Mr. SACCO. We are still looking for him.

Mr. ABERCROMBIE. That is what I meant. He or she hasn't contacted me. And I doubt that they will. So I don't think we are bound by fly-by-night outfits that are operating and that exploit foreign workers.

I don't take any pleasure in that. I am not coming after them. I think it is a situation, then, is it fair to say, Mr. Sacco, where unscrupulous people regardless of their nationality, regardless of where they are, are able to take advantage of a situation and people desperate to make a living, their families have to be fed, too, and they are being taken advantage of.

Mr. SACCO. Absolutely.

Mr. ABERCROMBIE. The last thing I want to ask is then on the serious transition program that we passed last year to enable the shipbuilders, I would like your view on that, to be able to pursue the shipbuilding initiative. Do you think that that is still something that we should pursue?

Mr. SACCO. Definitely, and we support it. I think there were a number of remedies and a number of suggestions that were made here that I think could help solve some of the problems that the American operators have. I mean, what was mentioned here was some kind of tax reform, accelerated depreciation, Coast Guard standards. I think if you put all of these together I think you can come up with a number, and maybe—I don't say that this is the answer, this may be a partial answer to the shipbuilding problem

that the American operator faces. I think there were some good suggestions made here.

Mr. ABERCROMBIE. Would you agree that reform legislation should include an operator component and a shipyard component?

Mr. SACCO. If you people introduce it, we will support it.

Mr. ABERCROMBIE. I am going to definitely quit while we are ahead on that, Mr. Chairman.

Mr. BATEMAN. Some more golden words uttered today.

Let me and if—

Mr. ABERCROMBIE. Mr. Chairman, excuse me would you yield to me?

Mr. BATEMAN. Quickly.

Mr. ABERCROMBIE. The mention was made that you have been here all these different years. And you had people in front of you who said they want to do the right thing, and they did. I honestly believe that Mr. Bateman is absolutely on the level about this being a bipartisan thing, and that 14 years under his leadership we can do something this year, and it is his intention to do it. And we are here to help him and not get in his way.

Mr. BATEMAN. More golden words.

Let me ask if you at the witness table would furnish us with any suggestions you have as to how we might do things that would require higher standards on the part of foreign-flag operators. If their standards are raised, the differential that we are seeking to make adjustments for would be smaller and whatever resources fiscally we have available will do more to keep more American-flag operators operating. So any suggestions you have as to how we might do—have an impact upon that we would be very receptive to.

Mr. BATEMAN. We have another vote, I am told that we are voting on voting to table an appeal of the Chair. I have no idea what mischief has been created, but I guess we have to go do our thing.

If you gentlemen would be kind enough to respond to any questions that I, Mr. Abercrombie, Mr. Kennedy or other members of the panel come up with for the record, we would be delighted if you would do that. If you have other testimony you want to give, I will be delighted to come back and hear you further, but I don't want to detain you unnecessarily.

So I will leave it to you, I will come back for further proceedings if you have other things that you want to send this way, otherwise, we will send you questions for the record.

Mr. SACCO. OK. We will do that, Mr. Chairman.

Thank you, very much.

[Whereupon, at 4:30 p.m., the subcommittee was adjourned.]

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